United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLEE

75-1004

To be argued by
FRANKLIN B. VELIE

United States Court of Appeals

FOR THE SECOND CIRCUIT

Docket No. 75-1004

UNITED STATES OF AMERICA,

Appellee,

—v.—

ANTHONY M. NATELLI and
JOSEPH SCANSAROLI,

Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR THE UNITED STATES OF AMERICA

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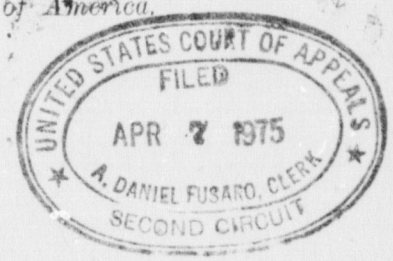

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United States Court of Appeals

FOR THE SECOND CIRCUIT

Docket No. 75-1004

UNITED STATES OF AMERICA,

Appellee,

—v.—

ANTHONY M. NATELLI and JOSEPH SCANSAROLI,

Defendants-Appellants.

BRIEF FOR THE UNITED STATES OF AMERICA

Preliminary Statement

Anthony M. Natelli and Joseph Scansaroli appeal from judgments of conviction entered in the United States District Court for the Southern District of New York on December 27, 1974, after a four week trial before the Honorable Harold R. Tyler, Jr., United States District Judge, and a jury.

Indictment 74 Cr. 43 was filed January 17, 1974. Count 2 charged Natelli and Scansaroli with preparation of false and misleading financial statements in a proxy statement required to be filed with the Securities and Exchange Commission, in violation of Title 15, United States Code, §§ 77ff and 78n, and Title 18, United States Code, § 2.*

* Four other defendants named in Count 2 and in other counts of the Indictment—Cortes W. Randell, Bernard J. Kurek, Dennis

[Footnote continued on following page]

Trial began on October 21, 1974 and ended wich guilty verdicts on November 14, 1974.

On December 27, 1974, Judge Tyler sentenced Natelli to serve 60 days of a one year term, the balance to be served on probation, and imposed a fine of $10,000. Scansaroli was sentenced to serve 10 days of a one year term, with the balance to be served on probation, and to pay a fine of $2,500.

Statement of Facts

Introduction

The proof disclosed that Natelli and Scansaroli, as outside auditors and accountants, unlawfully prepared materially false financial information for inclusion in a 1969 proxy statement of their client, National Student Marketing Corporation ("NSMC"). Their primary motive was to cover up the fact that inaccurate and misleading financial information included in NSMC's 1968 annual report only months before had been improperly and unprofessionally certified by them as auditors and that subsequent events had shown that report to be wholly unreliable.

In auditing the NSMC 1968 annual report, Natelli, the partner in charge of the audit, and Scansaroli, the audit supervisor, made entries to NSMC's books long after year end which changed a large loss for the year into an even larger profit. The adjustment booked, as "sales" and "assets", $1.7 million of "unbilled accounts receivable." These were anticipated earnings NSMC hoped to obtain when it performed services for its clients in the future. In booking these "sales", the defendants, Natelli and Scan-

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M. Kelly and Robert C. Bushnell—pled guilty to one or more counts prior to commencement of the instant trial. A seventh defendant, John G. Davies, was severed, and subsequently pled guilty, after two days of trial, to the conspiracy count of a superseding indictment, 74 Cr. 985.

saroli, at management's request, bypassed proper audit steps.

Only five months after the annual report, over $1 million of these "sales" were written off as nonexistent or uncollectible, and virtually the entire balance remained unbilled and uncollected.

The defendants expressed the fear that their improper auditing, if revealed, could mean the loss of their licenses to practice as certified public accountants. Natelli and Scansaroli took steps to cover up the losses. In writing off the uncollectible sales, Natelli and Scansaroli improperly netted the losses with a newly "discovered" tax credit; and in a proxy statement * prepared to facilitate the acquisition of several companies for NSMC stock, they took further steps to conceal the write-offs. In the proxy statement, Natelli and Scansaroli erased all narrative disclosures of the write-offs from proxy statement drafts, and they totally buried the resulting losses by improperly subtracting them from a column of unrelated figures, the figures for later-acquired subsidiaries.

The Government adduced expert proof that in doing these things, the defendants repeatedly violated generally accepted accounting principles. The defendants called eight accountants (besides themselves) to the stand. However, none of them gave evidence to rebut this proof. On this appeal, in the more than 200 pages of briefs filed by the defendants, their firm, and their professional association, as *amici*, nowhere is the proof of these violations of generally accepted accounting principles even mentioned.

Defendants, bound by their fears to NSMC's service, went further. In preparing the earnings statement for the first nine months of 1969 in the proxy statement, Natelli and Scansaroli helped suppress disclosure of an additional $1 million in 1969 write-offs (the "Pontiac contract") by

* This proxy statement was the subject of the indictment.

plugging the resulting hole in the earnings with yet another post-period adjustment (the "Eastern contract"). This adjustment surfaced under bizarre circumstances at the printer's plant while the proxy statement was actually in preparation.

The proxy statement did not disclose NSMC's losses, or the write-offs of over $2 million in sales known to Natelli and Scansaroli. Instead it portrayed NSMC as a profitable and growing company. The upshot was that, thanks to Natelli and Scansaroli, NSMC was able to fool the owners of large companies with genuine earnings into selling their companies in exchange for NSMC stock.

Chronological Summary

1. The 1968 Audit

In 1968, NSMC was a new and small company in the business of delivering promotional and advertising materials to students by direct mail, by tacking up posters on campus, and the like. (GX 5, p. E38) * NSMC's fiscal year ended August 31 of each year, and thus the first quarter ended on November 30, the second on February 28 and the third on May 31. (Tr. 138).

In August of 1968, just before year-end, NSMC's relationship with its prior auditors terminated, and it hired Peat, Marwick, Mitchell and Company ("PMM") as outside accountants and auditors. PMM's first task was the 1968 year-end audit. Natelli was the partner in charge of the audit; Scansaroli supervised the field work, and performed much of the audit work himself (Tr. 137-145).

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* "Tr." refers to transcript pages found in appendix vols. I-IV with identical numbering. "GX" refers to Government exhibits; "NX" and "SX" refer to Natelli and Scansaroli's exhibits, respectively. Page number references for exhibits are to the page numbers in the Exhibit Volume of the appendix, except where otherwise indicated.

The trial balances prepared by PMM accountants from NSMC's books, some two months after the end of the fiscal year, disclosed a loss of over $80,000 for the year (Tr. 714-5; GX 4C at p. E33). A schedule prepared by Bernard Kurek ("Kurek"), NSMC's comptroller, showed an even larger loss of $232,000 for the year. (GX 1; Tr. 148). After learning these facts, Cortes W. Randell ("Randell"), NSMC's president, informed Natelli and Scansaroli of further "sales" not previously included in NSMC's records. These were described as oral commitments by advertisers to use NSMC services in the future. Though it was nearly two months since the end of NSMC's 1968 fiscal year, Randell requested that NSMC be permitted to book as 1968 earnings virtually all of the anticipated profits from these oral commitments to use future services on the theory that NSMC had already performed the "work" of designing the marketing programs for these "sales". (Tr. 151 et seq; 1829, GX 2).

Natelli and Scansaroli acceded to Randell's request and made an accounting adjustment to the books of NSMC for the year 1968. Their adjustment booked as sales and assets of NSMC for 1968 $1.7 million of these "unbilled accounts receivable." (GX 3; GX 4C at p. E34; Tr. 712-717) The adjustment turned NSMC's loss into a very handsome profit—more than double the profit shown in the preceding year. (Tr. 181-189; GX 5 at p. E54).

Natelli and Scansaroli made the adjustment, and certified the resulting profitable financial statements, despite the fact that they knew, as to almost the entire amount, the following facts:

(1) These "sales" were not based on legal binding contracts. Indeed Scansaroli noted in his workpapers, in assessing the new method of accounting pressed for by the client, "Under this method extra caution should be used because there is no legal binding contract." (GX 3 at p. E3)

(2) The only records of such "sales" available to Natelli and Scansaroli were reports by NSMC's own salesmen of oral commitments by NSMC clients to use NSMC services in the future. These reports were prepared on October 17 and 18, 1968, months after the "sales" supposedly had been made and the fiscal year had ended. (GX 3 pp. E10 et seq)

(3) No expenditures had been made by NSMC which could be attributed to any of the "work" NSMC was claiming to have performed during the course of the preceding fiscal year. Indeed, in booking these "sales" and determining what portions were earnings, Natelli and Scansaroli, months after the year ended, had to estimate (and accrue) every penny of cost. (Tr. 723-4; GX 4B at p. E31).

(4) No services had yet been performed which obligated any client to pay NSMC any money (Tr. 1665, 1668). In fact, Natelli and Scansaroli determined that NSMC salesmen were not even entitled to commissions for any such "sales" (GX 4C, p. E32; Tr. 1974).

(5) NSMC had never previously accounted in this fashion for any material amount of "sales" (GX 3, p. E4),* and, indeed, there were no unbilled accounts receivable at all on NSMC's books prior to this adjustment (Tr. 721).

(6) NSMC had never demonstrated any ability to perform work of this kind on this scale. (GX 3, p. E4).

(7) The adjustment was extremely material, as it transformed a large loss into a still larger profit (twice the size of the prior year's reported profit) (GX 5 at p. E54).

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* Natelli's long recitation of the work of a prior NSMC accountant, Michael Sullivan, at pp. 7-8 of his brief, is disingenuous. Neither Natelli nor Scansaroli, in effecting a major change in the way NSMC accounted for its work, ever bothered to talk to Sullivan or to look at his work papers. (Tr. 1580-83, 1588, 1592, 1966-68).

(8) At Randell's urgings these "sales" were not audited by the traditional means—direct written confirmations mailed to the client—on the ground that written requests for confirmation might seem too pushy to NSMC's clients and might result in lost sales. (GX 2; Tr. 193).

Scansaroli himself acknowledged under oath before the SEC in 1971 his understanding that normal confirmation procedures might result in lost sales, stating,

> "What I am saying is that we got to a point *where we did not want to upset anybody or irritate anybody and they'd say forget about it. In this type of business it is touch and go* and therefore we decided we would not confirm them on a written basis." (Tr. 1607-8). (Emphasis supplied)

Again, in the Grand Jury, Scansaroli stated:

> "The reason for not confirming them in writing was that it was a special type of situation, where the salesmen were dealing with these various clients and they were at the point that they thought that if they pushed the clients too hard, that they would stick them in the back some place, or they may say we are busy, we don't have time to sign the contract. *They felt it was a touch and go situation between the account executive and the people he was dealing* with. In many cases it was also with the ad agency. They didn't want to push the ad agency because the ad agency in this case had some power as to who would do the advertising." (Tr. 1601-2). (Emphasis supplied)

In short, Scansaroli knew that NSMC had not even secured the business for itself. He proceeded to "confirm" the sales through telephone "confirmations" of the flimsiest sort (see below).

Similarly, Natelli, the auditing partner, told Kurek, NSMC's comptroller, in late October, 1968, that even though he recognized that these "sales" had first surfaced two months after year end, that the company had not yet performed any billable work, and that without the "sales" there would be a loss, nonetheless, the "sales" would be reported to the public in the annual report. Natelli stated, "It is a young company and without it it could kill the company." (Tr. 181-2).

The NSMC annual report for 1968, which issued on November 15, 1968, showed glowing economic health and growth for NSMC. However, as Natelli and Scansaroli both knew, without the late-booked $1.7 million of unbilled "sales", a large loss would have been shown. (GX 3 at p. E4; GX 65-2, at E411 and also annexed to this brief).

The defendants certified the annual report even though they were aware of NSMC's aggressive acquisition policy and of the fact that NSMC's stock was selling at a high earnings-per-share multiple (Tr. 1953-4). Following the issuance of the 1968 report (and prior to the proxy statement in September of 1969) an additional seven companies were acquired largely for NSMC stock and in reliance on the 1968 annual report. (Tr. 197-9)

2. The Falsity of the 1968 Report Becomes Manifest

As early as December 9, 1968, Natelli learned from Kurek that NSMC still had not received any written contracts or letters of commitment, or been able to bill anything, on the $1.7 million of sales booked as of the year which had ended the preceding August. (Tr. 206-7). Natelli expressed alarm and demanded a meeting with Randell. There he stated that at the next audit, no sales would be booked unless "firm enough to confirm in writing." (GX 7; Tr. 208) By late April or early May of 1969, only five or six months following the issuance of the 1968 annual

report, NSMC had written off over $1 million of the $1.7 million in "sales" booked and audited by Natelli and Scansaroli.

During this time, NSMC had begun preparation of the proxy statement which was the subject of the indictment, and both Natelli and Scansaroli were at work on it. In late April or early May, Kurek (by then NSMC's chief financial officer) and John Buck, NSMC's new comptroller, met with Natelli and Scansaroli. Kurek stated that he had met with Randell, reviewed unbilled "sales" and had decided to write off certain of them as uncollectible. A schedule of the unbilled "sales" in question was turned over to Natelli and Scansaroli. (GX 13 at p. E103). The schedule showed that NSMC had already written off $350,060 of these sales by subtracting them from their current year's figures. An additional $678,000 (bringing the total write-off to in excess of $1 million) of these previously-reported "sales" were to be written off, and Kurek and Buck asked Natelli and Scansaroli how to design the write-off. The following day, Scansaroli brought Buck a paper with the write-off on it. (Tr. 633-644). This write-off was adopted by NSMC and placed in its general ledger (GX 11 at journal voucher entries, E93-95).

The entry wrote off $678,000 of sales retroactively, that is, as a deduction from 1968 sales. However, the 1968 earnings were not reduced because the entry just happened to include an unrelated tax credit in the exact amount to the penny of the profit written off. (Tr. 645; GX 11, journal voucher 283 at E95; GX 13 at p. E98). Scansaroli explained to Buck that they had just discovered an error in the 1968 deferred tax computation, and therefore the credit was available. (Tr. 645-6, 663-4).

Subsequent to the SEC's investigation into the affairs of NSMC, Scansaroli and Natelli told the SEC that the tax credit had been an error after all. (Tr. 1373-76).

In examining the witness Buck, Natelli's counsel sought to elicit testimony that the form of the write-off was proper, and offered a chart (NXM) to illustrate that it simply combined several accounting steps into one entry. However, counsel withdrew the offer of the chart when Buck testified that in his twelve years as a certified public accountant he had never before or since seen such an entry. (Tr. 665-670). The unrebutted proof in the case showed that it was a violation of Accounting Principles Board Opinion No. 9, and therefore a deviation from generally accepted accounting principles, to net, as Scansaroli had done, an extraordinary item (the tax credit) with an unrelated ordinary item (the write-off of sales and profits). (Tr. 1307).

At the very time that Natelli and Scansaroli (and the NSMC accountants) wrote-off these $1 million of 1968 sales, they became aware of six additional uncollectible "sales" totalling $177,547 which were "bad" or "to be written off." Scansaroli collected the information as to these uncollectible "sales" and included in it his work papers on May 22, 1969. (GX 13 at pp. E102, E104, E105; Tr. 736-741; GX 65-15 at E422 and also annexed to this brief).

Also, at the same time, NSMC added to the figures for the first half of the year (a period which had closed two months before but for which NSMC was just then releasing figures) an unbilled "sale" of over $1 million to the Pontiac Division of General Motors. Like the $1.7 million in "sales" retroactively booked the prior October, this $1 million "sale" converted what Natelli had been told on March 8, 1969 (right after the six-month period closed) was a losing operation into one reporting a profit. (Tr. 222-223; GX 10A, GX 40). On May 22, 1969, the day Scansaroli placed in his work papers schedules showing that NSMC had written off over $1 million in 1968 sales, and that an additional $177,000 was no good, Scansaroli also

placed in his work papers a letter from Pontiac as "back up" for the million-dollar-plus "sale". The letter was dated two months after the close of the accounting period. (GX 13 at p. E106).

Also on May 22, 1969, Scansaroli initialled a form in his proxy workpapers which certified that he had inquired "into all matters raised at the time of our audit on which the lapse of time might shed additional light." (GX 13 at p. E100).

At approximately this time, Scansaroli told Kurek and John Stalick, NSMC's budget director, that he was concerned about the unbilled "sales", and "that he didn't know whether the right decision had been made back in August, and he was concerned about his CPA certificate. He [Scansaroli] also said, 'Perhaps I ought to put it in a locked box in a bank.'" (Tr. 237-8). At trial, Natelli conceded that Scansaroli had made such comments to him several times at the time of the $1 million write-offs. (Tr. 2032-8, 1933-1933A).

On June 3, 1969, a few weeks after the million dollars in write-offs, the appearance of the post-period Pontiac "sale", and the discovery of an additional $177,000 of bad 1968 "sales", Natelli met with Kurek. Natelli told Kurek he was "very concerned about the situation" and that "people working under him are uncomfortable with this situation and *if anything were to happen, their certificates and careers would be at stake.*" (Tr. 233-234 and GX 14).

Because of Natelli's concern, Kurek invited him to the next NSMC Finance Committee meeting, which took place on June 9, 1969. At that meeting, Kurek brought with him charts, reviewed at the meeting, which analyzed the history to that date of certain of the unbilled accounts receivable "sales" of NSMC. (Tr. 238-9). The charts (GX 15) showed that of the $1.5 million of 1968 "sales" analyzed

on the charts, approximately $900,000 had been written off. Of these, $670,000 were "sales" of NSMC salesman Ronald Michaels; another $200,000 were "sales" of another NSMC salesman, Bernard Ganis. Also, a third NSMC salesman, Jack Siadek, had accounted for $213,000 of 1968 "sales", none of which, according to the chart, had as yet resulted in any billing by NSMC or collection of any revenues, even though it was now more than nine months after the 1968 year had ended.

During the course of the June 9, 1969 Finance Committee meeting, Natelli and NSMC officers discussed the unbilled receivables. A stenographer present at the meeting made a transcript of some of the discussion (GX 16). Excerpts from the transcript revealed the following. Randell noted the fact that approximately $1 million had been written off. Replying to Randell's claim that the write-offs were largely attributable only to the salesman Ron Michaels, Don Fergusson, the NSMC executive then in charge of the sales force stated "it's the system of booking, not the man." Natelli noted that "3.3 [million dollars] is sitting unbilled," and that the "total volume of sales for '69 has yet to be performed . . . all sitting unbilled." When James Joy, NSMC's acquisition specialist, declared that because of several acquisitions, the company showed larger numbers, Natelli responded ". . . fine but it's important that 3.3 [million dollars] is unbilled in [the] balance sheet. Suppose we do run into problems . . . will you sue them . . . doubt if you have a case." (GX 16). Natelli also complained of NSMC's practice of post period adjustments which were used to increase the earnings of periods already closed, stating "that when we got to the end of a quarter . . . a contract or two are slipped in at the last minute." (Tr. 245-6). At the close of the meeting, the parties agreed to compromise, and Randell declared "Tony doesn't want to see the company stabbed." (GX 16; Tr. 238-246).

3. The Proxy Statement

In August of 1969, with NSMC's year-end in sight, work accelerated on the proxy statement required for NSMC's acquisition of four large groups of companies, including the well-known travel companies of Arthur Frommer and the large, publicly-held, genuinely profitable insurance companies of Interstate National Corporation ("INC"). The Frommer acquisitions were for stock and some cash; the other acquisitions were entirely for NSMC stock. (GX 25, pp. E170; E183-185; E191; E195-196).

A. The False Footnote (Paragraph 3 of Count Two)*

As part of the proxy statement, Natelli and Scansaroli set about to draft a footnote reconciling the company's prior reported earnings, including those from the 1968 report, with the historical summary contained in the earnings statement in the proxy. The latter included in it the addition of later acquired and pooled earnings. This footnote was the *only* place in the proxy statement which permitted an interested investor to see what NSMC's performance had been in its preceding fiscal year, 1968, apart from the earnings and sales of the companies it had recently acquired in fiscal 1969.

In the course of preparing the footnote, Scansaroli subtracted $678,000 of the written-off NSMC 1968 sales from the figures for later acquired pooled companies instead of from NSMC's own figures.** (GX 13, p. E97; GX 17; Tr. 890, 891, 904). Natelli knew that this had been done,

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* The Indictment contained two specifications of fraud. The first related to a footnote to the audited earnings statement for 1968. The second related to the unaudited statement of earnings for NSMC's then most recently ended period, the nine months ended May 31, 1969. The jury was properly instructed that proof of either allegation would support a conviction.

** These were the same bad sales whose loss Scansaroli had already improperly netted against the tax credit.

and substracted an additional $70,200 of NSMC 1968 sales losses from the pooled companies. (Tr. 890-3, 2061-8). The unrebutted testimony was that this subtraction of a total of three quarters of a million dollars of NSMC losses from a column of unrelated figures was improper and without any warrant in accounting (Tr. 1315, 692-3, 567).

Natelli himself scratched out all narrative disclosure of the write-offs, so that there was no disclosure in the footnote (or anywhere else in the proxy statement) that over 1 million (over 20%) of previously reported NSMC 1968 sales had been written off. (GX 17; Tr. 562-567, 1198-1211; GX 65-9; and GX 65-10, at p. E416-418 and also annexed to this brief). The unrebutted proof showed that this prior period adjustment which Natelli and Scansaroli had effected without any disclosure that such an adjustment had been made was in violation of Accounting Principles Board Opinion Number 9, and therefore in violation of generally accepted accounting principles. (Tr. 1304-1308).

B. The False Nine Month Earnings Statement (Paragraph 4 of Count Two)

On the afternoon and evening of August 14, 1969 the INC board of directors met with the defendant Randell in Chicago to agree on the NSMC acquisition proposal. Approval had to wait since the then available draft of the proxy statement did not have in it the earnings for NSMC's first three quarters of 1969 (the period ended May 31, 1969). (Tr. 1038-1043)

In order to close the deal, Randell left the Chicago meeting, flew to Washington, D.C. in his private jet, and picked up Natelli, Scansaroli, Kurek, Buck and Stalick. He then flew them to the Pandick Press in New York City to finish proxy statement. (Tr. 250-3, 651-2).

In the course of preparing the figures, at approximately 3:00 a.m., Natelli, in the presence of Scansaroli, told Randell that the $1 million Pontiac "sale" would have to be written off. Randell coolly replied that he had a "commitment" from Eastern Airlines in a similar amount attributable to the nine month period. That period had ended over two months before. (Tr. 257-9) Randell then called Kelly, the salesman whose $1 million Pontiac "commitment" was to be written off, and asked him to come to the printing plant. (Tr. 258-263, 651-655). Kelly arrived several hours later, during the daylight hours, with a "commitment" letter from Eastern Airlines, dated August 14, 1969 but purporting to represent a $820,000 commitment entered into in May, that is, just prior to the end of NSMC's nine-month period. (GX 18).*

The circumstances surrounding the Eastern "sale" were described by Natelli as "weird" in a memorandum prepared at the printer's (GX 21). Scansaroli acknowledged he thought it "strange" (Tr. 1709). This switch represented the third post period juggling of NSMC's books known to the defendants. The first had been the booking of $1.7 million of 1968 sales two months after the close of the year. The second was the $1.2 million Pontiac sale booked as earnings of the first six months of 1969 two months after that period closed. In all three cases, the common thread was that by last-minute discovery of unbilled "commitments", NSMC was able to transform a loss into a large, publicly-reported profit.

By the time of the third such juggling, Natelli and Scansaroli were not only familiar with this modus operandi but also knew full well that the "sales" that had surfaced under these circumstances had ultimately proven bad. For

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* Kelly's uncollectible million dollar Pontiac "sale" had been backed up by a similar letter, similarly produced two months after the close of the period to which it was said to be applicable. (GX 12).

with the write-off of the Pontiac "sale", of the $3.3 million of the unbilled accounts receivable booked in the period from year-end 1968 through the first half of 1969, $2 million had been written off to the knowledge of both defendants. (GX 65-14, at p. E421 and also annexed to this brief).

On Saturday, August 16, 1969, the next day following the incident at the Pandick Press, Douglas Oberlander, an accountant at PMM, in performing his "SEC review" came upon the additional $177,000 in 1968 "contracts" earlier in May found to have been no good by Joseph Scansaroli but still not written off. Oberlander found still more "contracts" to be no good as well. Oberlander called Kurek at home. Kurek told Oberlander to see him on Monday, August 18. Oberlander did so, and brought with him a schedule of uncollectible or nonexistent 1968 "sales". The bad contracts on Oberlander's schedule, minus contracts which were then and there written off, together with the bad contracts previously noted by Scansaroli, totalled over $320,000, above and beyond the more than $1 million in 1968 contracts that had previously been written off. (Tr. 1222-28; GX 65-15) Kurek refused to talk to Oberlander, and instead asked for Scansaroli. Scansaroli, after discussing the matter with Natelli, agreed not to change the proxy statement to reflect these additional bad sales. (Tr. 263-272, 2093-2097, 747-764). Oberlander declined to simply initial the SEC review which certified that he had inquired into all matters on which the lapse of time since the audit might shed light. Instead, Oberlander noted on the form that those matters had been covered in discussions among Scansaroli, Randell and Kurek. (GX 13 at tp. E107; Tr. 762-767) As a result, the nine month earnings statement in the proxy statement not only included "earnings" from the Eastern "sale", but also was not adjusted downward to reflect the additional $320,000 of known uncollectible sales.

The proxy statement was filed on September 30, 1969. (GX 25; Tr. 1089-90). There was no disclosure in it of the fact that NSMC had written off $1 million of its 1968 sales (over 20%), and over $2 million of the $3.3 million unbilled "sales" it had booked in 1968 and 1969. Nor was there any disclosure of the fact that without unbilled receivable, NSMC had no profit in 1968, and no profit in the first nine months of 1969. (GX 65-2; Tr. 1221).

Within two weeks, NSMC consummated the acquisition of three of the four groups of companies which were the subject of the proxy statement, largely for NSMC stock. The closing of the fourth, and largest group, INC, was scheduled for October 31, 1969. (Tr. 277-8).

In October of 1969, Scansaroli went to work for NSMC. There, he worked up schedules showing how many companies would have to be acquired in order to overcome NSMC's projected $2 million dollar loss for 1960 and achieve Randell's oft-made public prediction that NSMC, having "doubled" its earnings in 1968, would "triple" its earnings in 1969. In one of these, noting NSMC's deepening losses, Scansaroli penned a note to Kurek: "Bernie, suggest you buy that shirt company as soon as possible." (Tr. 1719-1723; GX 53*).

4. The Comfort Letter

NSMC's acquisition agreement with INC, by far its largest acquisitionee, required that PMM deliver, on the day of the merger closing, a "comfort letter" assuring INC that there had been no adverse developments in NSMC's financial picture since the date of the contract signing in August. (GX 25, p. E279)

Natelli delegated a PMM staff accountant to prepare the comfort letter. The accountant, John Johnston, promptly found the bad unbilled accounts receivable which had been brought to Natelli and Scansaroli's attention on August 18, 1969 by Douglas Oberlander, $177,000 of which

* Not printed in Exhibit Volume of Appendix.

had been known to Scansaroli since May. Johnston also concluded that other adjustments were necessary. Johnston and his immediate superior, Bill Colona, drafted a very somber comfort letter, containing $884,000 of downward adjustments. (GX 26*; Tr. 926-934). It did not, however, contain the entire story. That was known only to Natelli and certain employees of NSMC including Scansaroli. Natelli, of course, knew of the Pontiac write-off and thus knew of an additional $1 million dollars of loss not disclosed in the comfort letter. Natelli also knew of the "weird" Eastern "sale". Natelli knew of the track record of the company's earnings as based upon "unbilled accounts receivable," of which $3.3 million had been booked, and over $2 million had been written off. And Natelli knew that decisions had to be reached that day as to whether the INC acquisition could go through, and whether PMM's general counsel or its professional practices partner would reveal NSMC's comfort letter adjustments to the SEC. Natelli did not disclose what he knew to his superiors at PMM. As a result, INC's representative, although startled by the comfort letter they did receive at the closing, did not get the whole truth in context, and thus permitted the deal to close. (Tr. 1056-1061). The fraud was completed.**

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* Not printed in Exhibit Volume of Appendix.

** At the end of the brief, are reproduced GX 65-2, GX 65-10, GX 65-11, GX 65-14 and GX 65-15 in evidence, which summarize and illustrate the facts proved at trial. GX 65-2 shows the materiality of the 1968 unbilled accounts receivable to NSMC as without them, the company had a $65,000 loss, but with them, reported a $388,000 profit. GX 65-10 places side by side an early draft of the false footnote, Natelli's handwritten changes, and the final footnote as changed by Natelli. GX 65-11 summarizes the omissions and misstatements in the final version of the false footnote. GX 65-14 summarizes the performance of NSMC on the unbilled accounts receivable during 1968 and the first half of 1969, showing the amounts written off and known to be bad or uncollectible. GX 65-15 summarizes the contracts uncovered as bad by Scansaroli (J.S.) in May 1969, rediscovered by Oberlander (D.H.O.) in August, 1969, and disclosed by Johnston and Colona in the comfort letter.

The Defense

(a) General Defense

As a matter of general defense, the defendants each called character witnesses. Two testified for Natelli, three testified for Scansaroli, and one testified for both. In addition, Natelli elicited information regarding other accounting services performed during the NSMC engagement which restricted NSMC management's claims of profit with respect to matters unrelated to the Indictment.

(b) Motive (The 1968 Audit)

Both Natelli and Scansaroli sought to contest the Government's argument that the proxy statement was a cover-up of their unprofessional work in the 1968 audit by asserting the propriety of their accounting work in 1968.

Scansaroli at first claimed that he had done everything he could to audit the contracts in progress. (Tr. 1608, 1611-12).

Further cross-examination extracted concessions from Scansaroli that:

(1) Scansaroli had lost direct control of the confirmation procedure by permitting NSMC salesmen to dial the phone to reach the person to be contacted (Tr. 1612-13);

(2) Scansaroli failed to confirm with the "contract" debtor (Tr. 1614);

(3) Scansaroli had unwittingly spoken to NSMC's printing contractor in the belief he had contacted an advertising agency (Tr. 1614 *et seq.*, and 1621-2);

(4) Scansaroli failed to keep adequate work papers (Tr. 1624-6);

(5) Scansaroli failed to examine NSMC salesmen's time records and instead simply assumed any work done had been done before the August 31 year-end (Tr. 1628);

(6) With respect to the Clairol "sale", the largest of the "sales" booked ($500,000 of the $1.7 million booked at year end 1968), Scansaroli apparently never asked to see a proposal by NSMC or any work-product at all produced by NSMC for Clairol (Tr. 1650);

(7) Scansaroli booked as $138,000 of "sales" a "commitment" from Syntex Corporation which specified no amount of money whatever and no obligation by NSMC or Syntex to perform or pay for any services, and which was dated two months after year-end, called for NSMC to make a proposal thereafter as to what services NSMC might perform, and contained a complete money back guarantee from NSMC to Syntex. (Tr. 1657-60; GX 3 at E29-30).

Finally, after lengthy cross-examination, Scansaroli conceded that rather than having done "everything possible," he had, instead, been "far too easily satisfied." (Tr. 1660).

Natelli, the partner in charge of the audit, authorized the use of telephone confirmations; however, he explained that he did not read in detail the workpapers which revealed the above facts (Tr. 1975, 1972).

(c) Defendants' False Testimony

With regard to the substantive matters at issue at the trial, the defendants gave testimony which was so self-servingly inconsistent with the documentary evidence and with their own pre-trial testimony as to warrant incriminatory inferences. Among the more flagrant examples were the following:

Scansaroli had twice, before trial, testified that the reason telephone confirmations (rather than the traditional written confirmations) were used during the 1968 audit was that he knew the situation was "touch and go" i.e., that NSMC had not yet assured itself that it had firm

commitments from the clients. This testimony (quoted earlier in this brief) was given before both the SEC in 1971 and the Grand Jury in 1973. However, at trial, Scansaroli admitted that if the situation was touch-and-go he should not have booked the sales at all, and gave new excuses for his poor confirmation procedures. When confronted with his prior testimony, Scansaroli claimed that his memory had improved. (Tr. 1600-03, 1607-08).

Natelli denied at trial that on December 9, 1968 he had told a roomful of NSMC employees (and Scansaroli) that thereafter, NSMC could only book commitments if they were "firm enough to confirm in writing." Natelli's denial on the stand was directly contradicted by a memorandum, prepared the day after the statement, which quoted him as above, and which was sent to all NSMC salesman for their guidance. (Tr. 209, 1995-9; GX 7).

Scansaroli emphatically denied, at trial, having told anyone—even in jest—that he feared losing his certificate to practice as a CPA. (Tr. 1572, 1679-81) This evidence was flatly contradicted by the unequivocal testimony not only of Kurek (as corroborated by GX 14) but even of Natelli that Scansaroli had made such comments not once, but several times (Tr. 237, 2032-8, 1933-1933A).

Natelli denied having told Kurek that the "people working under him are uncomfortable with this situation [unbilled receivable accounting] and if anything were to happen, their certificates and careers would be at stake." This denial was completely inconsistent with a memorandum prepared the day of the conversation, quoting him as above, which was sent to the president of NSMC to inform him of this important concern. (GX 14; Tr. 233-4, Tr. 2027-9). In addition, Natelli conceded on cross-examination that the write-offs had been "professionally embarrassing." (Tr. 2029) Natelli also denied any recollection of making the statements at NSMC's June 9, 1969 finance committee meet-

ing quoted earlier in this brief, and disputed their plain import despite the fact that the quotations were taken from a verbatim transcript of portions of the meeting made by a secretary who was there taking shorthand notes (GX 16; Tr. 238-246; 2013 *et seq.*).

The defendants offered mutually inconsistent versions with respect to the circumstances surrounding the tax credit. Thus, while Scansaroli had told the SEC, under oath in 1971, that only he and Natelli had been involved in the calculation of the tax credit (Tr. 1686), Scansaroli told the trial jury that the tax credit was "in effect" computed by Carol Raimondo, a PMM tax department employee. (Tr. 1687) Mrs. Raimondo testified that she did not calculate the tax credit. (Tr. 1396).

Neither defendant could properly account for the fact that there were no work papers in existence showing the calculation of the tax credit. Scansaroli emphatically testified that there were no calculations made in arriving at the tax credit and therefore no workpapers had ever existed. (Tr. 1687-9) This was flatly contrary both to his own prior sworn testimony before the SEC (Tr. 1688) and to Natelli's testimony that there had been calculations but that he could not find the workpapers. (Tr. 2044).

(d) Consultations With Otkiss, the SEC Reviewing Partner

By way of alibi, Natelli claimed to have cleared the nondisclosure of the 1968 write-offs with PMM's SEC reviewing partner Leon Otkiss (Tr. 2193).*

However, it appeared from the cross-examination of Otkiss and Natelli that Natelli had deceived Otkiss by not

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* Scansaroli had testified in the Grand Jury that he and Natelli had decided "on their own hook" not to disclose the write-offs (Tr. 882-884a).

giving Otkiss the critical facts needed in order to evaluate the question. Thus, Natelli told Otkiss that there were write-offs of up to $700,000 of sales but omitted to state the additional facts known to him that $1 million of 1968 sales and an additional $1 million of 1969 sales had been written off, and that virtually the entire balance of the company's unbilled receivable sales were uncollected and uncollectible. Natelli further deceived Otkiss by stating that the sales write-offs resulted from the unethical acts of a single salesman, Ronald Michaels,* omitting to state the facts known to him that other salesmen's sales totalling approximately $1.3 million dollars were also written off as no good. (Tr. 1764-70; 2082-90).

(e) The Comfort Letter

Natelli claimed that his good faith was apparent from the disclosure of certain NSMC losses in the INC comfort letter, delivered some four weeks after the filing of the proxy statement. To establish this claim, Natelli called four PMM employees, Otkiss, Colona, Holton and Earle.

As noted above, from their testimony and Natelli's it appeared that one John Johnston, a PMM staff accountant, uncovered in the course of his work during September, 1969 certain "bad" or uncollectible contracts previously noted by Scansaroli in May of 1969 and again brought to Scansaroli's and Natelli's attention by another PMM staff accountant, Douglas Oberlander, in August of 1969. Johnston uncovered other problems in NSMC's books and reported them all to his immediate superior William Colona. Colona and Johnston then drafted a comfort letter stating adjustments

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* The defendants never explained how the "unethical acts" of Michaels which NSMC had told them about — taking kickbacks from NSMC's *suppliers* — in any way resulted in the invalidity of the commitments Michaels had brought in from NSMC's *clients* (purchasers), where no kickbacks could be involved.

which completely wiped out NSMC's 1969 first three quarter earnings as stated in the proxy statement. When confronted with this state of facts, Natelli told Colona to call Otkiss the next morning, the day of the closing. (Tr. 1780-86; 912-13; 917-936). Otkiss recommended bringing Holton, a member of PMM's professional practices committee, into the discussions. (Tr. 1940). Holton, in turn, consulted with PMM's legal counsel Victor M. Earle, III. During the course of the day, two amendments to the comfort letter were suggested underlining the seriousness of the adjustments. Neither of these was suggested by Natelli. (Tr. 1802-5; GX 67*).

One of the topics under consideration during the day was whether to go to the SEC.** When consulted as to whether to bring the facts to the attention of the SEC, Natelli had a meeting with Scansaroli, at that time an NSMC employee, and then told his superiors the adjustments were the results of "honest mistakes." (Tr. 2103-6; GX 67). At no time did Natelli tell his superiors, including the SEC review partner and the firm's general counsel, that an additional $1 million dollars had been secretly written off during the first three quarters of 1969 (the period which was the subject of the comfort letter) and not disclosed anywhere. Nor did Natelli tell his superiors that overall write-offs of unbilled receivables totalled over $2 million out of $3.3 million booked, that the $1 million Pontiac commitment had been written off, or that the Eastern Airlines contract had suddenly surfaced under "weird" circumstances at 3:00 a.m. while the proxy statement was being printed up. Accordingly, the SEC was not informed of the facts, the comfort letter did not contain the facts, and the INC board permitted their company to be acquired for NSMC stock.

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* Not printed in Exhibit Volume of Appendix.

** Natelli did *not* claim as he has suggested in his brief at pp. 34 and 41 that he himself recommended going to the SEC (Tr. 1945, 2102-2103).

(f) Accountant Testimony

Defendant Natelli called eight witnesses. Six of these were certified public accountants, and one of the CPA's was, in addition, a university professor of accounting. Scansaroli called five witnesses, of whom three (including one who also testified for Natelli) were CPA's. One of these was a college professor of accounting. Including the defendants, then, no fewer than ten certified public accountants testified for the defense. Not one of these offered any testimony to rebut the Government's proof that Natelli and Scansaroli had deviated from generally accepted accounting principles by

(1) subtracting $750,000 of written-off 1968 NSMC sales from the figures for other, later acquired, companies (Tr. 1315, 692-3; 567;);

(2) netting the extraordinary item for a newly discovered tax credit against the write-off of some of the NSMC 1968 sales losses, an ordinary loss item (Tr. 1307); and

(3) failing to disclose the concededly * material post-period adjustment which resulted from writing off retroactively $750,000 of 1968 sales. (Tr. 1304-1308; 690-692).

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* Natelli conceded that accountants do not adjust a prior period's figures unless the adjustment is material (Tr. 2123). Buck's testimony was to the same effect. (Tr. 692). Both the retroactive write-off of $750,000 in sales and the tax credit were prior period adjustments.

ARGUMENT

POINT I

The Evidence Was More Than Sufficient To Support The Jury's Guilty Verdicts As To Both Defendants.

Both Natelli and Scansaroli claim that the evidence was insufficient to support the jury's verdicts of guilty as to them. These claims are wholly without merit. Both defendants omit to disclose to this Court in their briefs important segments of the Government's proof. For example, neither defendant has mentioned the Government's uncontested expert testimony that both defendants, in preparing the false proxy material, violated generally accepted accounting principles in three different and important respects. Defendants' failure to discuss this proof here renders their arguments frivolous. As neither defendant has adequately stated the facts proved at trial, for the Court's convenience, the facts are briefly re-summarized below, in chronological order, as to each defendant separately. These facts show that the jury was fully justified in its verdicts.

1. The proof as to Natelli

The jury was amply justified in finding that Natelli wilfully made, caused to be made, or aided and abetted in the making of the materially false footnote and the materially false nine months earnings statement.* The proof is summarized, below, in chronological order.

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* The jury was properly instructed that it could return a verdict of guilty if satisfied of the proof as to either the allegation concerning the footnote or the allegation as to the nine-months earnings statement (Tr. 2340).

(a) The 1968 Audit

Natelli was the partner in charge of the 1968 audit of NSMC. As such, Natelli personally agreed to adjust NSMC's books, long after year end, to add $1.7 million of newly found "sales." Natelli knew that this adjustment changed NSMC's loss into a large profit (Tr. 181-2).

Natelli directed that those sales were to be audited by telephone after management complained that the more usual procedure—written confirmations—might result in NSMC losing the sales (GX 2; Tr. 193; 1838-9; 1607-8; 1601-2). Natelli stated that he had neglected to read carefully the work papers which disclosed Scansaroli's complete failure to audit the sales properly (Tr. 1972). Within a period of months, Natelli learned that over $1 million of these $1.7 million of "sales" had been written off, and that the balance were uncollected and uncollectible. The jury was entitled to consider the above facts as providing a powerful motive to cover up those losses.

(b) The write-offs

In late April or early May, 1969 Natelli, with Scansaroli, was informed that NSMC had written off approximately $345,000 in 1968 sales, and wanted to write-off an additional $678,000 of these sales. Natelli and Scansaroli were asked, by NSMC accountants, how to accomplish this write-off (Tr. 633-9). The write-off which Natelli and Scansaroli designed did not result in any reduction of published NSMC earnings, as it improperly netted the lost earnings against a purportedly newly discovered tax credit (Tr. 645). The unrebutted expert proof was that it was a violation of generally accepted accounting principles to net the extraordinary item relating to the tax credit with the write-off of earnings, an ordinary item (Tr. 1307). The jury was further entitled to find the tax credit itself a fraudulent entry. The tax credit appeared at exactly the right time, and in precisely the right amount to absorb

the earnings loss relating to the sales write-offs. And when the SEC began to investigate, Natelli and Scansaroli acknowledged there was no such credit after all (Tr. 1373-6). Finally, the defendants' conflicting stories regarding this item of proof furnished further evidence from which the jury was entitled to conclude that the tax entry was part of the defendants' scheme to cover up.*

(c) The False Footnote (Paragraph Three of Count Two)

Three months later, in preparing the proxy statement, Natelli took further steps to bury the truth regarding NSMC's write-offs.

The historical earnings summary in the proxy statement was a "pro forma," or "pooled" statement (GX 25 at 21). That is, it showed NSMC's prior years as if NSMC had, during those prior years, owned certain businesses it had acquired in only the past few months. The footnote, which is the subject of paragraph three of Count Two, had as its function to reconcile NSMC's prior earnings as

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* Natelli argues at Point III (p. 75) of his brief, that it was reversible error to permit the Government to prove the fraudulent nature of the tax credit. This point is frivolous, as the false tax credit was inextricably bound up in the write-off of NSMC sales which the indictment alleged the defendants falsely omitted to disclose in the footnote. (GX 13 at p. E98). As Judge Tyler expressly found, ". . . the minute you get into those figures you have got to consider the tax figure." (Tr. Dec. 20, 1974 p. 15). In any event, this proof was admissible as evidence of the defendants' knowledge or intention to deceive. *United States* v. *Papadakis*, Dkt. No. 74-1847 (2d Cir., January 10, 1975), slip op. 1231, 1241; *United States* v. *Deaton*, 381 F.2d 114, 117 (2d Cir. 1967); *United States* v. *Bozza*, 365 F.2d 206, 213 (2d Cir. 1966); Rule 404(b), Fed. R. Evidence. Natelli's argument is nothing more than a bold assertion that the Government must list in the indictment every item of its proof or suffer reversal. The law in this Circuit is settled to the contrary. *United States* v. *Koss*, 506 F.2d 1103, 1113 (2d Cir. 1974).

reported in the pooled historical earnings summary in the proxy statement with the figures previously reported to the public. It was the only place in the proxy statement which an investor might look at to examine the actual performance of NSMC, the core company, apart from other companies' earnings it had subsequently bought up with its stock.

In preparing this footnote of audited figures, Natelli omitted to disclose the fact that $1 million (over 20%) of NSMC's sales of its most recent year, 1968, had been written off. Instead, Natelli personally scratched out every reference to the fact that there had been write-offs (GX 17; Tr. 563-567; 1197-1211; GX 65-9 and GX 65-10). And in addition, Natelli deliberately subtracted NSMC's lost sales resulting from the write-offs from the later acquired companies' figures (Tr. 890-3; 2062-8). By so doing, Natelli deliberately overstated NSMC sales by $750,000 (15%); and understated the pooled companies by $750,000 (12%).

The Government proved without contradiction that this subtraction was wholly improper and a violation of generally accepted accounting principles (Tr. 1315; 692-3; 567). The Government further proved, by unrebutted expert testimony, that Natelli (and Scansaroli) had violated generally accepted accounting principles by retroactively writing-off sales without disclosure of the fact (Tr. 1304-8). This devastating proof fully justified the jury's guilty verdict. As this court stated in *United States* v. *Simon*, 425 F.2d 796, 807 (2d Cir. 1969), *cert. denied*, 387 U.S. 1006 (1970): "The jury could reasonably have wondered how accountants who were really seeking to tell the truth could have constructed a footnote so well designed to conceal the shocking facts."

(d) The False Nine-Month Earnings Statement (Paragraph Four of Count Two)

Before completing his work on the NSMC nine-month earnings statement, Natelli knew that NSMC had on three occasions juggled its books to add large earnings to periods long before closed. The first was when Natelli and Scansaroli booked $1.7 million of 1968 "sales" after year-end 1968. The second was when NSMC booked a million-dollar-plus "sale" to Pontiac as part of its six month report, months after that period closed. And the third was when Natelli and Scansaroli booked the Eastern "sale" as part of the nine-months statement, months after the period had closed (Tr. 2056-7). The effect in each case was to very materially improve NSMC's earnings picture just as it was about to be made public.

Natelli knew from the circumstances surrounding the Eastern "sale" that it was fraudulent. The "sale" was first announced at 3:00 A.M. at the printer's plant where the proxy statement was being printed, and it emerged just in time to plug a hole in the earnings statement caused by the Pontiac write-off. In a memorandum prepared at the Pandick Press, Natelli noted: "To go and *replace* G.M. contract with this would be really wierd [sic]." (emphasis in the original) (GX 21; Tr. 257-63; 651-55). Natelli knew that NSMC had booked, and had announced to the public, $3.3 million of unbilled accounts receivable "sales" while secretly writing off over 2 million of them. Natelli knew that virtually the entire balance was uncollectible (GX 16; Tr. 238-246; GX 65-14). Natelli knew that an additional specified several hundred thousand dollars in "contracts" were no good and should be written-off. In his memorandum prepared at the Pandick Press, Natelli noted "Seem to be problems 100-200 m on other contracts, we have not previously discussed. Would be very material

to results" (GX 21; Tr. 2093-4).* Natelli knew that NSMC's salesmen had proved repeatedly unreliable and that the salesman, Kelly, who suddenly produced the Eastern "commitment" letter, dated three months after the alleged "sale", was the same salesman responsible for the deficient Pontiac commitment. Finally, Natelli knew, as early as March, 1969, that NSMC would have a loss of over $1.5 million without certain acquisitions and unbilled sales which Randell hoped to obtain (Tr. 222-3; GX 10A).

Natelli, despite his knowledge of these facts, participated in the preparation of the nine-month earnings statement. In view of Natelli's inclusion in this statement of the Eastern contract, and his refusal to take out the known bad contracts, the jury was amply justified in finding this earnings statement deliberately false.

Natelli argues, at p. 47 of his brief, that the Government failed to prove that the Eastern contract was in fact not earnings of the first nine months of 1969. This argument overlooks the facts, proved by the Government, that NSMC had no record of expenditures on this "contract", no record of ever having billed Eastern for services on this "sale," and not one scrap of paper from Eastern other than the suddenly-produced letter (which was never checked with Eastern) to indicate Eastern's interest in such a sale (Tr. 572, 1149-50). In the circumstances, this was more than sufficient to meet the Government's burden that it was false and misleading to book Eastern as sales and earnings for the period ending in May, 1969. The Govern-

* Natelli argues at p. 50 of his brief "the Government offered no testimony that Oberlander's workpapers were brought to Natelli's attention"; and that "there was no evidence that any of these [bad sales noted by Oberlander] were called to Mr. Natelli's attention." This argument is misleading in the extreme, and it omits the proof on the point. Natelli's knowledge of the bad contracts which Oberlander had scheduled was proved by Natelli's memo (GX 21) and Natelli's admissions at Tr. 2093-4.

ment repeatedly offered further proof that the Eastern "sale" was written off as bad only months after the proxy statement was filed, but on defendants' objection, the Court would not permit this proof in evidence. (Tr. 845 et seq.). From the facts proved, however, the jury was amply justified in concluding the NSMC had never sold anything to Eastern or earned anything having to do with this "contract" as of May, 1969.

(e) False and Evasive Testimony

The jury was amply justified in discrediting Natelli's testimony as false and evasive. Natelli's testimony was completely inconsistent with contemporaneous documents, which quoted him and which were made under circumstances attesting to their reliability (GX 7, 14, 16; Tr. 1995-9, 2028; 2013 *et seq.*). Based on this evidence and the demeanor evidence, the Government argued:

> "What about Mr. Natelli's credibility. Bear in mind your own impressions of Mr. Natelli when he testified on cross-examination. The Government submits that you are entitled to find from his demeanor on the stand that that man was incapable of giving a single straightforward truthful answer. Ask yourselves how many times did he just wander off and have to be told what the question was again. Ask yourselves was he giving you a line of double talk. Ask yourselves was he telling you the truth. Because maybe you noticed and the Government submits that Mr. Natelli has a magical memory, a convenient memory. It's hazy on the things that tend to show his guilt and yet it's very firm and postive on the points he wants to make here, even after five years, and even when it is plainly inconsistent with documents prepared at the very time of the events in question such as Government's Exhibit 7, about the

December 9 meeting, Government's Exhibit 16 about the June 9 meeting, and Government's Exhibit 14 about the June 3 meeting.

Mr. Natelli's testimony, in short, is just completely inconsistent with the rest of the proof. Ask yourselves if any other witnesses in the case behaved in this fashion. Ask yourselves did the defendants act as if they were telling the truth.

Look, there were conflicts in the proof. The defendants tell one story. The Government's proof, documentary proof in evidence, tells a completely different story. You are just going to have to decide this case by resolving the conflicts in the proof. Use your common sense. Ask yourselves who has the biggest motive to fabricate, to hide, to cover up and deceive here. Just ask yourselves about that.

Ask yourselves why the defendants' stories are utterly inconsistent with documentary proof. Documents don't change their story. Once they are prepared, there they are.

The Government contends in short that the defendants set about to bring the cover up right here into this courtroom, right there to the witness chair. The Government submits that they perjured themselves to cover up what it is that they did.

Again, if you find that they gave false statements, you are entitled to find that they did so because they knew that they were guilty.

The Government submits, in short, that you can't believe these defendants. If you can't believe them, you must convict them (Tr. 2311-14).

No objection was made to this argument. Indeed, none could have been made, as the defendants' credibility was the

key issue before the jury in the case. As Judge Tyler put it, in addressing the defendants at their sentencing:

> "The tragedy is that two things, without more, in this case I am sure enabled the jury to reach its verdict. One was the workpapers which you made. Two was your own testimony on the stand." (Tr. of December 27, 1974 at p. 13).

(f) Materiality

Natelli argues at p. 42 of his brief, that his omissions and misstatements in the proxy statement were immaterial. This argument is frivolous. NSMC had no earnings in 1968 without unbilled accounts receivable (Tr. 1184-87; GX 65-2). And NSMC, even after all of its acquisitions, had no earnings in the first nine months of 1969 without unbilled accounts receivable (Tr. 1221). The proxy statement recited that "fixed fee contracts" (unbilled accounts receivable) were the most "profitable" aspect of NSMC's business (GX 25, p. 16). Natelli knew the facts which showed that the unbilled receivables were wholly nonexistent and fraudulent. Natelli knew of the three occasions NSMC had juggled its books to add profits to periods long closed. And Natelli knew that the "profits" were nonexistent as NSMC had booked $3.3 million of unbilled "sales" while secretly writing-off $2 million. Natelli's failure to disclose the facts known to him hid from the public the complete unreliability of NSMC's reports and permitted NSMC to masquerade as a highly successful enterprise when it in fact had severe losses. The jury was amply justified in finding the defendants' misstatements and omissions highly material.

2. The Proof as to Scansaroli

The jury was amply justified in finding that Scansaroli wilfully made, caused to be made, or aided and abetted the making of the materially false footnote and the materially false nine-month earnings statement.* The proof is summarized, below, in chronological order.

(a) The 1968 Audit

The jury was entitled to find that Scansaroli's incredibly lax and unprofessional audit of the $1.7 million "unbilled receivables" provided a powerful motive to hide the resulting losses in the later proxy statement.

Scansaroli was responsible for the auditing of the $1.7 million of unbilled accounts receivable, and carried out that "audit" personally (GX 3). Scansaroli knew that these "sales" had surfaced long after year-end and after NSMC's own books showed a loss for the year. Scansaroli knew that these "contracts" were highly material—the difference between a profit and a loss (Tr. 1661; GX 3, p. E4). Scansaroli knew that there were no records of these "sales" except for NSMC salesmen's memos of "oral" commitments by clients to use NSMC services in the future. These were all prepared long after year end and many of them were unsigned (GX 3, pp. E10 *et seq.*). Scansaroli knew that "extra caution" was warranted because the "sales" were not even based upon legal binding contracts (GX 3, p. E3).

Despite these facts, Scansaroli's audit was so unprofessional and lax as not to be an audit at all. Scansaroli consulted no time records or other employee records, but instead assumed that NSMC had performed work during the

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* The jury was properly instructed that it could return a verdict of guilty if satisfied of the proof as to either the allegation concerning the footnote or the allegation as to the nine-month earnings statement (Tr. 2340).

1968 year (Tr. 1628). Scansaroli (together with Natelli) agreed not to confirm the "sales" in writing because he knew that this might result in NSMC losing the sales (Tr. 1601-2, 1607-8).* Instead, Scansaroli allowed NSMC personnel to dial the phone for him. He made no record, with respect to several of these "sales," of whom he spoke to, what was said, or even what number was dialed (Tr. 1622-6). The complete futility of these telephone confirmations is shown by the fact that with respect to two important sales, Scansaroli spoke to NSMC's printer in the belief that he had reached the clients' advertising agency (Tr. 1614 *et seq;* 1621-2).

In one instance, the Syntex "sale," a "commitment letter" was available. It was obvious that Scansaroli either failed to read it or disregarded what he had read. This letter did not commit Syntex to buy, or accept, or pay for, any NSMC services, and it mentioned no amount of money at all. Despite these facts, Scansaroli booked this as a $138,000 sale (Tr. 1657-60; GX 3 at p. E29-30).

(b) The Write-offs

Within five months, Scansaroli learned that NSMC had written off over $1 million of the "sales" which Scansaroli had supposedly audited (Tr. 633-9). In addition, Scansaroli learned that an additional $177,000 of these "sales" were no good, and that virtually the entire balance had not been billed or collected (GX 13, pp. E102, E104, E105; Tr. 736-741; GX 65-15). At that time, Scansaroli told Kurek and Stalick on one occasion, and Natelli on several occasions, that he was concerned that he might lose his professional license to practice as a CPA (Tr. 237-8, 2032-8; GX 14). Again as noted Scansaroli, at trial, denied having

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* As noted, Scansaroli, at trial, departed from his previous sworn testimony before the grand jury and the SEC to deny this fact.

made these statements (Tr. 1572; 1679-81). The jury was entitled to find from this false denial further proof of his guilty knowledge and intent.

At the time of the write-offs, Scansaroli took steps to hide the facts. When requested to design an entry writing-off the three largest of these "sales," Scansaroli produced an entry which resulted in no reduction of published NSMC earnings (GX 13 at p. E98), by netting the loss from the write-offs against an unrelated and newly found tax credit which was in exactly the right amount to absorb the loss (Tr. 645; GX 11, Journal Voucher 283 at E95). John Buck, NSMC's former comptroller, testified that in his twelve years as a CPA he had never seen an entry like it before or since (Tr. 666-670). The entry was improper and in violation of generally accepted accounting principles, as it netted an extraordinary item (the tax credit) against ordinary items (the lost earnings) (Tr. 1307). The defendants adduced no expert testimony to rebut this proof.

The jury was entitled to find the circumstances surrounding the tax credit further evidence of criminal intent. The tax credit surfaced at just the right time and in precisely the right amount to absorb (by virtue of the improper netting) every penny of loss and thereby avoid disclosure of the loss. Further, the tax credit turned out to be nonexisten after the SEC began its investigation. And finally, Scansaroli's testimony was inconsistent with his own prior sworn testimony before the SEC and with other proof in the case regarding the tax credit.

Thus, Scansaroli told the SEC under oath that he and Natelli had computed the tax credit (Tr. 1686). At trial, he departed from that testimony and told the jury that Carol Raimondo had computed it (Tr. 1687). Mrs. Raimondo denied having computed the credit (Tr. 1396). Scansaroli was unable to explain the highly unusual cir-

cumstances as to how the extremely complicated tax credit was computed without any workpapers evidencing the calculations. Scansaroli told the SEC that there had been computations and that there were workpapers (Tr. 1688). At trial, he stated emphatically that there had been no computations and, thus, no workpapers (Tr. 1687-9). His co-defendant Natelli contradicted this statement, testifying that there had been computations, but that he could not find the workpapers (Tr. 2044). The jury was entitled to find Scansaroli's trial testimony false and consider it as further evidence of guilty knowledge.

(c) The False Statements in the Proxy Statement

First, the proof overwhelmingly showed that Scansaroli prepared the false statements in the proxy himself. John Johnston, a former PMM accountant who worked on the proxy statements testified:

> Q. Do you recall whose function it was to take numbers from the working papers and actually do the numbers in the proxy statement drafts, place them in there as being the numbers which were to appear?
>
> A: My contact with the proxy statement and the work that was being done on the proxy statement, *to my knowledge, Mr. Scansaroli was inserting the numbers in the proxy draft.* (Tr. 904). (emphasis added.)

Scansaroli did not controvert this testimony. The other available proof was to the same effect. (Tr. 650-1; 250). Thus, the workpapers underlying the false footnote figures were in Scansaroli's writing (GX 13 at p. E97), and the unrebutted testimony was that Scansaroli was responsible for the figures which were placed in the false nine-month earnings statement (Tr. 2051; 650-1). This fact was further borne out by Oberlander's testimony that it was Scansaroli who directed him to prepare the entries in the nine-month proxy figures which switched the newly discovered

Eastern "sale" for the written-off Pontiac "sale". (Tr. 768-9).

Second, the proof was overwhelming that Scansaroli intended to deceive:

(i) The False Footnote

The jury was entitled to find from the unrebutted evidence that, in preparing the footnote, Scansaroli himself improperly subtracted $678,000 of NSMC losses from a column of unrelated figures, the figures for later acquired subsidiaries. The workpapers used to calculate the figures to be inserted in the false footnote set out the figures for each of the later acquired subsidiaries, and figures representing "adjustments and reclassifications." In this column were the 1968 NSMC sales written off retroactively. The entire workpaper was in Scansaroli's handwriting (GX 13 at p. E97). When these figures were inserted into the proxy draft from Scansaroli's workpaper, the NSMC sales losses were subtracted from the other companies' figures. Natelli acknowledged that this was "probably" done by Scansaroli (Tr. 890).* Scansaroli did not deny having made the subtraction (Tr. 1692-3) and, as shown above, Johnston testified that it was Scansaroli who "was inserting the numbers in the proxy draft" (Tr. 904).

The Government proved without contradiction that this subtraction was wholly improper and a violation of generally accepted accounting principles (Tr. 1315, 692-3, 567). From it the jury was entitled to find an intent to deceive.

Scansaroli acknowledged that he and Natelli decided, on their "own hook", against disclosure of the adjustment they had made to NSMC's previously reported 1968 earnings (Tr. 884-884A). The Government proved (and Natelli ac-

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* Scansaroli's brief inaccurately quotes Natelli as saying that it *"possibly"* was Scansaroli (Brief at p. 27).

knowledged) that this adjustment was material in accounting terms (Tr. 692, 2123). The Government proved that the failure to disclose it was a further violation of generally accepted accounting principles (Tr. 1304-1308). Neither defendant called expert witnesses to rebut this central and devastating proof. From this proof, the jury was fully entitled to find an intention to deceive.

(ii) The False Nine-Month Earnings Statement

By the time he prepared the nine-month earnings statement, Scansaroli knew that NSMC had, over the course of the preceding year and a half, booked, and published to the investing public, $3.3 million of unbilled receivable "sales"—and had secretly written off over $2 million of them (GX 65-14; Tr. 1217-19). Scansaroli knew that NSMC had, on three occasions, juggled its books by adding enormous earnings to periods which had long before closed. The first was after year-end 1968, when NSMC booked $1.7 million of unbilled "sales". As Scansaroli well knew, these had turned out not to be "sales" after all, as over $1 million had been written off, and another $300,000 were, to his knowledge, no good and uncollectible. The second occasion was when NSMC booked over $1 million of "sales" (the Pontiac "commitment") as part of its first half report, long after that period had closed (GX 13 at p. E106). As Scansaroli well knew, this "sale" was written off in its entirety only three months later (Tr. 768). The third occasion was the Eastern "sale" which Scansaroli caused to be booked in substitution for the written off Pontiac "sale" as earnings of the nine-month period. This was done two months after the period had closed.

Scansaroli was present when the Eastern "sale" was first proposed in order to plug a hole in the earnings caused by the write-off of the million dollar Pontiac "sale". This occurred at about 3:00 A.M. at the printer's plant

where the proxy statement was being printed up. The proof on this point was ample. Kurek testified that Scansaroli was present when Natelli and Randell discussed writing off the Pontiac sale and when Randell requested permission to substitute the Eastern "sale" for the Pontiac "sale" (Tr. 257-258). Scansaroli did not challenge or probe Kurek's version of the facts on cross-examination, and Scansaroli himself acknowledged on cross-examination that Kurek's account was correct (Tr. 1708). Kurek's version was also corroborated by Natelli (Tr. 1918, 2047-2051). Although Scansaroli, on his direct examination, denied knowledge of these conversations at the printer's plant, Scansaroli even then acknowledged knowing of the Pontiac-Eastern switch before it was carried out (Tr. 1561-2). In addition, Oberlander stated that it was Scansaroli who gave him the figures to accomplish the entry which at one stroke wrote off Pontiac and wrote on Eastern in the nine-month figures (Tr. 768-771). And Scansaroli had to acknowledge that he knew that switch to be "strange" (Tr. 1709).*

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* The Government, in summation, made a fair and reasoned argument, as follows:

> "Mr. Scansaroli tells you that he wasn't aware that Pontiac and Eastern were being switched at the Pandick Press.
>
> "Well, you evaluate that one on its face, because you will recall that Mr. Scansaroli is the man responsible for getting the figures into the proxy statement. That was his job. And that's what they were doing. Pontiac represented figures that either had to come in or go out and so did Eastern. It seems that everybody in the place was in on the secret except for Mr. Scansaroli. Buck knew it. He wasn't involved in it particularly. But he heard it all going on. Kurek knew it, Natelli knew it. Scansaroli tells you, 'Oh, I don't know anything about it.' You are entitled to find that a false denial, and you are further entitled, if you believe it a false denial, to consider that false denial important proof that he was denying it because he knew it was criminal." (Tr. 2311).

[Footnote continued on following page]

In addition Scansaroli knew that NSMC had on its books over $300,000 of additional "bad" sales. Scansaroli had known that $177,000 of these were bad since May 1969 (GX 13, at pp. E102, E104, E105; Tr. 736-741). The balance were brought to his attention by Douglas Oberlander (Tr. 751-762). The evidence showed that whenever PMM accountants other than the defendants learned of these uncollectible "sales", they made attempts to disclose them. Indeed, the moment Oberlander found the problem contracts, he called Kurek at home on a Saturday (Tr. 263-4). However, Kurek met with Scansaroli, and Scansaroli thereafter met with Natelli and decided not to change the proxy statement (Tr. 266-72, Tr. 2093-4). In complete contrast, two month, later, when Johnston and Colona found the bad "contracts," they promptly disclosed what they had learned in the comfort letter (Tr. 921 et seq., Tr. 279, 280; GX 65-15).

Despite his knowledge of all these facts, Scansaroli prepared the nine month earnings statement which stated that NSMC had over $700,000 in earnings. The nine month statement included the Eastern "sale," and left on the books over $300,000 of other "sales" Scansaroli knew did not exist. The jury was entitled to find this a knowingly false statement.

(d) False and Evasive Testimony

The jury was amply justified in discrediting Scansaroli's testimony, and in finding his false testimony further evidence of criminal knowledge and intent. Credibility was the central jury issue as to Scansaroli, as argued by the

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Scansaroli's trial counsel, who represents him on this appeal, made no objection to this argument at trial. However, here, in his brief, at p. 33 he states that this argument by the Government "shabbily distorts the record" in violation of the duties of a prosecutor. It is obvious, however, that it is not the Government which has imposed upon the Court in this regard.

Government and defense (Tr. 2309-11, 14; 2229) and noted by Judge Tyler (Tr. 12/27/74, p. 13). As shown above, Scansaroli departed from previous sworn testimony in important respects in his attempts to avoid conviction.

POINT II

The Trial Court's Instructions To The Jury Were Correct.

At the end of the case, Judge Tyler delivered a charge to the jury closely modeled on Judge Mansfield's approved charge in *United States* v. *Simon, aff'd,* 425 F.2d 796 (2d Cir. 1969) (Friendly, C.J.), *cert. denied,* 397 U.S. 1006 (1970). In so doing, Judge Tyler was on solid ground, since the instant case is similar to *Simon* and falls well within the factual and legal borders mapped in that case. Nonetheless, defendants, after plucking isolated parts of the charge rather than taking it as a whole as they should, *Cupp* v. *Naughten,* 414 U.S. 141, 146-148 (1973), *United States* v. *Pinto,* 503 F.2d 718, 724 (2d Cir. 1974), allege no fewer than eight errors in Judge Tyler's instructions (Natelli Brief, Points II A-G; Scansaroli Brief, Point IV). Not one of their points is substantial.

A. "Reckless Disregard"

Judge Tyler delivered, almost exactly verbatim, the "reckless disregard" charge delivered by Judge Mansfield in *Simon.* The charge in *Simon* was:

> "While I have stated that negligence or inadvertent error do not constitute guilty knowledge or intent, you are entitled to consider, in determining whether a defendant acted knowingly and intentionally, whether he deliberately closed his eyes to

> the obvious, or to facts that would certainly be observed or ascertained in the course of his duties, or whether he recklessly stated as facts matters of which he knew he was ignorant. If you find such reckless, deliberate indifference or disregard for truth of falsity, the law entitles you to infer knowledge therefrom; but such an inference, of course, must depend on the weight and credibility extended to the evidence of recklessness and indifference. Ordinary negligence, inadvertence or mistake would be insufficient to support a finding of guilty knowledge or intent."
>
> —(*Simon* transcript, pp. 3977-78).

Comparison of this instruction with the charge on knowledge in the present case (Tr. 2364-65) establishes that Judge Tyler's charge tracked the *Simon* language virtually word for word.

The *Simon* charge, in turn, was simply a reiteration of a principle and jury instruction that has been settled since *United States* v. *Benjamin*, 328 F.2d 854, 862-3 (2d Cir.; Friendly, C.J.), *cert. denied*, 377 U.S. 953 (1964), if not before, *Bentel* v. *United States*, 13 F.2d 327 (2d Cir.), *cert. denied*, 273 U.S. 713 (1926), and that has been repeatedly upheld by this Court: *E.g.*, *United States* v. *Frank*, 494 F.2d 145, 152-53 (2d Cir.), *cert. denied*, — U.S. — (1974); *United States* v. *Brawer*, 482 F.2d 117, 127 (2d Cir. 1973); *United States* v. *Jacobs*, 475 F.2d 270, 287 (2d Cir.), *cert. denied*, 414 U.S. 821 (1973); *United States* v. *Sarantos*, 455 F.2d 877, 880-882 (2d Cir. 1972); *United States* v. *Abrams*, 427 F.2d 86, 91 (2d Cir.), *cert. denied*, 400 U.S. 832 (1970). Without such a principle, a tremendous loophole would exist for a criminally complaisant accountant or attorney (not to mention one who commits more mundane crimes like the acquisition of stolen

goods) who seeks to circumvent ". . . criminal sanctions merely by deliberately closing his eyes to the obvious risk that he is engaging in unlawful conduct." *United States* v. *Sarantos, supra*, 455 F.2d at 881.

Natelli's claim (at pp. 57-8 of his brief) that the charge was fatally deficient for failing to add "with a conscious purpose to avoid learning the truth" to the requirement that the jury must find a "reckless deliberate indifference to or disregard for truth or falsity on the part of a defendant . . .", ". . . [that] a defendant . . . deliberately closed his eyes to the obvious or to facts that certainly would be observed or ascertained in the course of his accounting work or [that] he recklessly stated as facts matters of which he knew full well he was ignorant" (Tr. 2427), is without substance. This Court specifically held in *United States* v. *Sarantos, supra*, 455 F.2d at 882, that "the phrase 'reckless disregard of whether the statements made were true' and 'conscious purpose to avoid learning the truth' mean essentially the same thing." Judge Mansfield's charge in *Simon*, quoted above, does not contain the language "with conscious purpose to avoid learning the truth", and neither defendant here requested at trial that it be included. Natelli cites no case which has found the absence of such language to require reversal, and this Court has sustained instructions far less precise or complete in this aspect than those given by Judge Tyler here. *United States* v. *Gottlieb*, 493 F.2d 987, 994-995 (2d Cir. 1974).*

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* In *Gottlieb*, the defendant was convicted of falsely stating to his draft board that he was enrolled in the National Guard, thereby securing a deferment. In fact, Gottlieb was not in the National Guard, but his defense at trial was that he thought that he was when he made the statement. Judge Griesa's instructions on knowledge, which this Court expressly found sufficient, were as follows, in their entirety:

[Footnote continued on following page]

"Again, the words 'knowingly and wilfully' are almost selfdefining. An act is done knowingly and wilfully if it is done intentionally, deliberately and not because of mistake, accident, mere negligence or some other innocent reason. It is necessary that the Government prove that the defendant acted with an evil purpose, but it is not necessary that the Government prove that the defendant knew he was breaking a particular, specific statute or rule. Basically in this case, what the Government must prove on this element is either one of two things. One of these alternative things that the Government can satisfy its burden of proof by showing is that when the defendant made or caused to be made the statement to his draft board that he was a member of the National Guard, if you find he made that statement, one alternative thing the Government can prove and satisfy this element of wilfully and knowingly, that language of the statute, is to prove that the defendant knew that the statement was false, knew that he was not, in fact, in the National Guard when he said he was.

It would also be sufficient in the alternative for the Government to prove a somewhat different thing, but I think I should bring this to your attention, and pay attention closely.

It would be sufficient for the Government to prove and for you to find, if you did, that the defendant made the statement that he was in the National Guard when he didn't know whether or not he was in the Guard.

Let me put it this way:

If a person makes a statement in an official form that he is a member of a particular unit of the National Guard, he is representing that he has knowledge of the facts he puts down. Now, if he doesn't have knowledge, if he doesn't know whether or not he is in the National Guard but he still puts the information down on the official form, then he has made a deliberately false statement. If he wilfully blinds himself to the fact, then there is a wilful and knowing misconduct. So if you find that the Government has proved beyond a reasonable doubt that the defendant either, first, knew he was not in the National Guard when he submitted a statement saying he was, or, second, that he didn't know whether or not he was in the National Guard when he represented, in fact, he was, then the element of knowing and wilful conduct is satisfied (*United States* v. *Gottlieb*, Appellant's Appendix at 1006a-1008a).

Natelli's other argument (at pp. 51-7 of his brief), that the "reckless disregard" principle has no application to the facts of the present case, borders on the frivolous. Consider, for example, defendants' approval of the booking of the Eastern contract in place of the Pontiac contract. The facts, largely undisputed, were that immediately after Natelli had reached a final decision not to include the Pontiac figures in the proxy statement being put together at Pandick Press in the early morning hours of August 15, 1969, Randell suddenly began claiming that there had been a substantial commitment with Eastern since the prior May, and Dennis Kelly, the same salesman whose million dollar Pontiac contract was being written off, appeared later the same morning with a similar written "commitment" from Eastern. Natelli temporized and, finally, after seeing the NSMC proposal to Eastern and the time logs of an NSMC salesman relating to the making of the proposal, gave final approval to booking Eastern in place of Pontiac, with no proxy disclosure of the switch.

At trial Natelli's interpretation of this evidence was that, while at first suspicious of the Eastern commitment, he took what steps he thought necessary—consistent (he would now add) with the fact that he was only conducting a review, not an audit—to satisfy himself of the legitimacy of the "sale", and he was as surprised as anyone when it later turned out no good. However, the Government's contention at trial (and now) was far broader. Given NSMC's long history (already known to Natelli) of retroactively booking "commitments" that later proved no good, coupled with the extraordinary way in which this retroactive written commitment for $820,000 suddenly surfaced out of nowhere in the early morning hours conveniently just as the Pontiac contract that was the mainstay at NSMC's nine-month "profit" was being written out of the proxy, coupled with the fact that the man who brought it in, Kelly, was the same salesman who had been

unable to meet his claims with respect to Pontiac, coupled with the fact that the Eastern "contract" had never before even been mentioned to the auditors—given all this (and more), the Government argued that, in the words of *United States* v. *Frank*, *supra*, 494 F.2d at 152, "too many red flags were flying", and the jury could find Natelli knew what was going on. But, the Government argued, Natelli deliberately closed his eyes to all these suspicious circumstances and pretended to treat the Eastern "contract" as if it were just one more commitment brought in under normal circumstances.

Natelli testified that he checked the contract. However, his "check" — looking only as NSMC's own salesmen's documentation (the proposal and time-records) — was, as Natelli knew, purely cosmetic. These records, of course, showed merely what NSMC had *proposed* that Eastern buy and the hours spent *trying* to get Eastern to buy it. Even within NSMC's internal records, Natelli never requested or looked for any record that NSMC had actually performed some service for Eastern, or spent any money doing services for Eastern, or that Eastern had previously expressed any interest in the proposal. There were no such records.

The Government's argument was *not* that Natelli was departing from any generally accepted standard of (limited) review responsibilities in not checking further. This is a straw man raised by appellants to buttress their appeal (see point B, below). Rather, the Government at all times argued that Natelli knew from the moment the contract arrived that it was a phony; but he fraudulently chose to avert his eyes. The limited review responsibilities of which Natelli argues so much on this appeal was, in this contact, simply a handy excuse to keep himself unblemished by any further direct knowledge of the "commitment's" fraudulence. As this court asked about another professional's similar tactic in *United States* v. *Jacobs*,

supra, 475 F.2d at 280, "With all the suspicious circumstances here present . . . why did not [the defendant] take one of the simple means that would have led to revelation of the truth?" The answer, as the Government argued, was that Natelli, knowing that NSMC's acquisitions hung in the balance, did not want to be in the position of having been told the hard truth about the Eastern "contract". Later would be time enough, when the acquisitions were completed and the Eastern contract could be quietly written off retroactively, like all the other undisclosed, retroactive write-offs. For now, it was sufficient if he could keep from hearing the real facts, and so he deliberately blinded himself to the suspicious circumstances of the origin of the Eastern contract, pretended everything was "normal", and proceeded with the narrowest possible "check".

This was the Government's theory of Eastern, argued in one way or another from opening to summation. (See, *e.g.*, Tr. 54-56, 58, 65, 1145-50, 2054-59, 2268-9, 2286, 2295-98, 2359). On this ground alone, the Government was entitled to the "reckless disregard" charge as given.

Moreover, Eastern was just a high point in a pattern of deliberate, reckless disregard by the defendants. There was, for example, the schedule of sales that, though bad, were still on the books. Beginning in May and continuing through October, this schedule was repeatedly brought to the attention of Scansaroli and Natelli; each time, they treated it, out of context, as one of NSMC's "honest mistakes." Each time, they deliberately failed to accord it any significance—even though their fellow accountants (Oberlander, Johnston and Colona) did. But, instead, they looked the other way and permitted the proxy statement to be issued without reference to it or reflection of it.

This schedule of bad contracts, which kept surfacing under ever-more-suspicious circumstances, only to be swept under the rug by the defendants, was but one item in the long sequence of write-offs of supposedly good contract. Each time a write-off was made, NSMC had an "excuse" for it (Michaels' "misconduct" was just the first) and had a new "commitment" to substitute for it. The first time this sequence occurred, perhaps the defendants could have innocently been duped. But, the Government argued, when it happened a second time, and then a third time, only someone determined not to hear the truth could have taken NSMC's behavior at face value. Here, again, the Government was entitled to the "reckless disregard" charge. For as Judge Learned Hand said long ago in approving such a charge in the trial of an accountant for conspiring to prepare false financial statements:

> "It is true that all these instances, taken singly, do not prove beyond question that White knew that the statements which he prepared were padded with false entries; but logically the sum is often greater than the aggregate of the parts, and the cumulation of instances, each explicable only by extreme credulity or professional inexpertness, may have a probative force immensely greater than any one of them alone."

United States v. *White*, 124 F.2d 181, 185 (2d Cir. 1941).

B. "Audit vs. Review"

(i) The Charge was Appropriate on the Facts Proved

The proxy statement contained both audited 1968 year end figures and unaudited 1969 nine-months figures. The indictment clearly stated that the first were audited, the second unaudited (Tr. 2331, 2334). Although defendants mentioned this distinction to the jury, they never introduced any proof, expert or otherwise, as to any factual

difference between audit and review procedures. Having failed to offer any proof on the "more limited" procedures required of a review, Natelli now contends that Judge Tyler should have provided this proof for them by instructing the jurors on it as a matter of law. Natelli and two *amici* claim that his failure to so charge constitutes a silent revolution in the law that will have disastrous consequence for the accounting profession.*

The defendants, as noted, called ten certified public accountants to the stand. If it was an important element of their defense that the jury be aware that the 1969 nine-month earnings, being unaudited, were only subject to "limited" review procedure, defendants had ten opportunities to put those procedures before the jury. Having totally failed to do so they cannot now bootstrap that failure into a claim that the Court committed error in failing to take judicial notice *sua sponte* of those alleged limitations and present them to the jury.

(ii) Judge Tyler Gave the Charge Requested by the Defendants

Nor did defendants request any such charge at the time. The fact is that the charge, as given, incorporated the essence of the defendants' sole request on this issue, and neither defendant objected to the absence of the kind of detailed charge they now claim to have been entitled to. In particular, Judge Tyler made crystal clear what the issue for the jury was as to the figures both audited and unaudited:

> ". . . generally speaking the issue which you really have to focus on here can be stated in a relatively simple fashion: Did the defendants or either one of

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* The American Institute of Certified Public Accountants filed an amicus brief in *Simon* that contained the same dire prophecies.

> them knowingly and intentionally either prepare and submit *material misstatements* as to the financial position or financial operations for NSMC for the year of 1968, for which the figures were stated to be *audited,* or in respect to the figures for NSMC for the first nine months of 1969, which were, as I recall the proxy statement, labeled as *unaudited* figures." (Tr. pp. 2340-41; emphasis supplied)

This language covered the essence of the one and only Request to Charge on the question of audited vs. unaudited statements submitted by either defendant, namely, Natelli's Request No. 8 (submitted on almost the last day of this three-week trial). This requested that the Court charge, as to the unaudited statement of earnings for the nine months ended May 31, 1969, that "The defendants' only responsibility as to this statement was to be satisfied that, as far as they knew, the statement contained no misstatement of material facts."

(iii) Defendants Did Not Object to the Charge

Following the charge, the defendants' only objection on this point was to claim that Judge Tyler had failed to point out that the nine-months earnings statement was unaudited. Since in fact he had pointed it out, Judge Tyler declined to charge further (Tr. 2384).

(iv) Even Now, Defendants are Unable to Specify What The Charge Should Have Been

The charge defendants now claim should have been given—one that would have "distinguished [responsibility for an audit] from the auditor's far more limited responsibility with respect to the company's unaudited financial statements" (Natelli brief, p. 59)—is one they never asked for; nor do they cite any case in which it ever was given. And even now, in their briefs, neither the appellants nor their *amici* can seem to find agreement as to what level

of reduced responsibility applies to a review as opposed to an audit. Scansaroli's brief does not deal with the point. Natelli's, as noted, refers to "the auditor's far more limited responsibility with resepect to the company's unaudited financial statements" but neglects anywhere to state of just what that more limited responsibility consists. At trial, as also noted above. Natelli's request to charge as serted that the defendants' "only" responsibility as to an unaudited statement "was to be satisfied that, as far as they knew, the statement contained no misstatement of material facts." (This instruction was precisely the one given Judge Tyler.) But the amicus brief of the American Institute of Certified Public Accountants states flatly (at p. 15) that "The independent accountant's *only* responsibility is to insist upon correction of departures from generally accepted accounting principles known to him", a position already rejected by this Court in *United States* v. *Simon*, *supra*, 425 F.2d at 805-06. Still a third view is set forth by the amicus brief of Peat, Marwick, Mitchell & Co., which, while never venturing an express statement of what Judge Tyler should have charged the jury as to the appellants' limited responsibility for the proxy review, states (at p. 5) that:

> 'the limited extent of the accountant's responsibility and of the techniques to be applied is made clear as it was in the Interstate merger agreement included in the proxy statement: '. . . that on the basis of a limited review, but not an audit . . . (including all such procedures as they consider necessary under the circumstances in connection with such limited review), they have no reason to believe that the unaudited interim financial statements of NSMC as of May 31, 1969, and for the nine months then ended, were not prepared in accordance with accounting principles and practices consistent with those followed in the preparation of the August 31, 1968 audited financial statements or that any ma-

terial adjustments of such unaudited interim financial statements are required for a fair presentation of the results of operations of NSMC.'"

Given this conflict among the appellants and their *amici* as to just what are the standards for an unaudited review, Judge Tyler can hardly be faulted for instructing the jury on this point as requested by the defense below and for not embarking *sua sponte* on an inquiry unsupported by any proof at trial, the proper outcome of which is yet in dispute even between appellants and their *amici*.*

(v) Judge Tyler's Charge Does Not Extend The Law of Accountant Liability

In view of the extravagant language in the briefs of the defendants and their *amici*, it is well to point out that this case, far from constituting an extension of *Simon*, represents a rather more obvious instance of culpability by accountants. In *Simon*, the great bulk of expert testimony was to the effect that generally accepted accounting principles had been complied with, and the question was whether that was sufficient under all the facts and circumstances. In the present case, by contrast, there was not one iota of evidence of compliance with generally accepted accounting principles, let alone principles of ordinary integrity.** The Government's uncontradicted proof was not

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* Natelli argues (at p. 60 of his brief) that the jury might have believed that the defendants were required to confirm the Eastern commitment in writing. This is pure speculation. The Government made no such argument, nor did the Court charge or the Government ever argue that audit procedures were required with respect to the unaudited figures.

** Judge Tyler did not instruct the jury on any specialized duty on accountants to inquire or investigate, but rather on the simple obligation imposed by the securities law on accountants, lawyers, corporate officers and employees and anyone else—that they shall not knowingly make or cause the making of false assertions in proxy statements.

merely that defendants' 1968 audit was incredibly lax but, more particularly, that the footnote they prepared for the proxy to reconcile those audited figures with the fact of the write-offs was in contravention, in at least three different respects, with clearly mandated accounting principles governing the presentation of such figures (see p. 25, *supra*).

This case is unlike any of the authority cited by Natelli or the two amicus briefs in that here the defendants actually prepared the false statements themselves with full knowledge of the falsity. The defendants not merely "associated" themselves with the fraudulent footnote and earnings figures; they wrote them. It was not NSMC who suggested subtracting some of NSMC's write-offs from the pooled companies' figures; it was the defendants. It was not NSMC who came up with the phony tax credit or who suggested netting the remaining write-offs against the credit; it was the defendants. And as to the 1969 figures it was the defendants who not only permitted NSMC to include Eastern in the proxy figures under circumstances that would tax the credulity of even far less financially sophisticated persons, but who actually prepared the entry substituting Eastern for Pontiac. And it was the defendants who prepared the final 1969 earnings figures in the proxy knowing full well that those figures still included another $320,000 in worthless contracts which the defendants had been repeatedly told were no good.

This was not a case where NSMC was able to to slip a fraud by the accountants by virtue of the fact that, as to some of the figures, the accountants were only conducting a "review", though as to others they were conducting an "audit". Rather, this was a case where the accountants themselves knowingly and wilfully designed the fraudulent cover-up of NSMC's real position.*

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* As the author of *Fischer* v. *Kletz*, 266 F. Supp. 180 (S.D.N.Y. 1967), Judge Tyler was both fully cognizant of the fact of some difference between responsibility for an audit and

[Footnote continued on following page]

C. When Eastern Was Booked

Natelli argues, (Point II-C of his brief) that the Court misstated the Government's contention with respect to the booking of the Eastern commitment. This argument is without merit. The Court properly stated the Government's contention (see II-A of this brief): that Natelli fraudulently agreed to go along and accept Eastern in place of Pontiac from the moment Kelly produced the "commitment letter" (if not earlier), but that he thereafter went through a charade of "checking" it. While Judge Tyler, in addition, mistakenly said that the witness Buck had given evidence that the actual paperwork in booking Eastern was performed then and there, that error was completely harmless in view of the fact that the jury remembered the evidence to be different, and thereafter requested, and had read to them, the testimony which bore on the issue, including Buck's. (Tr. 2403).*

D. Focusing on the Footnote

The appellants complain of Judge Tyler's charge at Tr. 2369:

> "Perhaps the critical issue in the case, therefore, can be summarized as follows: Were the quoted earnings figures and footnote set forth in Count 2 fairly set out?"

Appellants argue that, so far as the 1968 audited figures were concerned, this sentence "directed the jury's attention to the footnote alone, whereas the issue to be considered was whether the audited financial statements as a whole

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for a review and also aware that the issue was irrelevant to the present case where, in contrast to *Fischer*, the accountants here wrote and booked in the proxy the footnote and figures complained of.

* Natelli's further complaint that *too much* evidence was re-read disregards the jury's request as reflected in the colloquy between the Court and the jury foreman at Tr. 2403-4.

fairly presented the financial condition of the company." (Natelli Brief, p. 65). But that is not correct. This portion of the charge did no more than point the jury to the threshold question: were the indictment's specific allegations of falsity correct.

The indictment did not charge the proxy statement as a whole with being false and misleading. It said that two specific parts of it—footnote D (paragraph 3 of the indictment) and the 1969 earnings figures (paragraph 4 of the indictment)—were false and misleading, that is, not fairly set out. The charge complained of simply stated in a single, straightforward sentence the basic issue framed by the indictment itself. That this was only intended as a starting point is made clear by the next paragraph of the charge: "If you determine that there is nothing materially false or misleading about this information as alleged in Count 2, that would end your inquiry and you would be obliged to acquit both defendants." (Tr. 2369-70).

Defendants' reliance on the portion of the *Simon* opinion approving Judge Mansfield's statement that the critical test in that case was whether the financial statements as a whole fairly presented the financial position of the company, 425 F.2d at 805, is misplaced. All *Simon* said with respect to this portion of Judge Mansfield's charge was that "The critical test according to the charge was the same as that which the accountants testified was critical", 425 F.2d at 806, so that the defendants there had no cause to complain. And the fact is that, even in *Simon*, when Judge Mansfield reached the part of his charge related to the footnote at issue there (*Simon* transcript pp. 4021-28), he gave the same kind of charge as Judge Tyler did here, to wit:

> "The issue presented for your determination is whether or not, in indicating in footnote 2 the possibility of netting, if not flatly assuming netting, the defendants acted knowingly and deliberately with

> intent to defraud or whether they acted in good faith and on the mistaken assumption that netting might be a possibility." (*Simon* transcript p. 4028).

In any case, defendants' complaint on this issue, as on many others, suffers from their having taken a single sentence of Judge Tyler's charge out of context, isolated it, magnified it, and thereby distorted it. Defendants complain, for example, that the sentence in question could have misled the jury into judging the materiality of the footnote from too narrow a frame of reference. But the sentence in question was preceded by several pages of charge on materiality that gave the appellants everything they now claim they were deprived of. Specifically, Judge Tyler charged on materiality as follows:

> "I want to define here for you what the law means about material facts.
>
> Let me approach it for you in this way. In deciding whether a fact is material, ladies and gentlemen of the jury, you are entitled to consider whether it was the kind of information that *a financial statement* ordinarily contains in order to fulfill *its function of fairly presenting the financial picture of the company* for which it is filed.
>
> A material fact can be simply defined as one that would matter to a reasonable person in deciding whether or not to purchase NSMC's stock, for example. That is to say, a fact, the validity of which would concern a reasonable person in making his purchase or investment decision.
>
> Obviously *a balance sheet or income statement* is not supposed to contain all the information a creditor or potential investor or stockholder might need or want to know in order to make informed judgments. The function of *the financial statement* is simply to present a basic summary of the company's financial position and operations and earnings for the time period stated.

> Now, in this connection I point out to you and I should have made this point earlier, but I think you understand it, no one is contending, and it certainly is not the fact, that an outside auditing firm such as PMM has responsibility for the operations or management of a company such as NSMC. An auditor must ascertain that *the financial statement* in question, such as the figures or the footnote, *fairly presents the results of the operations and the financial position of the company.* Also, as stated heretofore, in effect, an auditor must honestly believe that *the financial statement or statements* are neither false nor misleading in respect to material facts." (Tr. 2368-69; emphasis supplied).

This lengthy prelude to the single sentence defendants complain of surely gave it a different coloring from the one they now ascribe to it. Having heard all this, no reasonable juror could have imagined that he was to somehow judge the materiality of the footnote in isolation from the rest of the "financial picture of the company" set forth elsewhere in the proxy.

E. Subjective Materiality

Natelli argues (at p. II-E of his brief) that the charge was defective as it omitted to instruct the jury that the defendants must be found to have known their misstatements were material. This argument is frivolous. No objection was raised below; Judge Tyler in fact gave this instruction repeatedly; and even if he had not, there is no authority or policy to suggest that knowledge of materiality is an element of the offense.

Natelli's argument flies in the face of this Court's repeated distinguishing of "materiality" and "culpability" as independent elements in securities fraud cases. *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp.*, 480 F.2d 341, 362-3 (2d Cir.), *cert. denied*, 414 U.S. 924 (1973).

As this Court said there, "The materiality test is concerned only with whether a prototype reasonable investor would have relied." 480 F.2d at 363.

The fact that this is a criminal prosecution does not of itself mandate that the defendants have knowledge of every element of the crime. *United States* v. *Feola*, — U.S. —, 43 U.S.L.W. 4404 (March 19, 1975). The need to show "*mens rea*" and the appropriateness of invoking criminal sanctions are more than satisfied by the existing requirement that the defendants be shown to have knowingly and deliberately lied, *cf. United States* v. *Schwartz*, 464 F.2d 499, 508-510 (2d Cir. 1972), *cert. denied*, 409 U.S. 1009 (1973), and the materiality element simply serves to limit both prosecutions and civil suits to violations that are of objectively demonstrable substantiality. What possible policy would be served by permitting accountants to knowingly lie with impunity about material matters so long as they thought their purposeful, deliberate lies were only about immaterial matters? As this Court said of an analogous claim in *Simon*: "We do not think the jury was also required to accept the accountants' evaluation whether a given fact was material to overall fair presentation . . ." (425 F.2d 806).

In any event, defendants can hardly complain on this point, since, once again, Judge Tyler gave them everything they asked for (and more than they were entitled to). Judge Tyler flatly stated that "A finding of an *intention* to include false and misleading information *of a material nature* is required" (Tr. 2364), and later restated the same thing in terms of auditor's duty, "[A]n auditor must honestly *believe* that the financial statement or statements are neither false nor misleading in respect to *material facts*." (Tr. 2369) (emphasis supplied). Finally, for good measure, he summed it all up in the following terms:

> "If you determine that there is nothing materially false or misleading about this information as alleged in Count 2, that would end your inquiry and you would be obliged to acquit both defendants. On the other hand, should you find that the quoted material is substantially inaccurate and misleading in whole or in part, then you would have to turn your attention to each of the defendants to consider what the evidence shows that he did or failed to do and to determine whether or not he participated in a scheme to *knowingly and intentionally* permit the submission of earnings figures *known to be false in a material way* to the SEC in the proxy statement." (Tr. 2369-2370; emphasis supplied).

That this was everything the defendants could reasonably desire on this point is shown by the fact that, while Scansaroli had specifically requested a (one-clause-long) charge on a defendant's knowledge of materiality, neither defendant took any exception to the charge as given (Natelli Brief, p. 71). In the light of the many careful exceptions to the charge taken at the time by both defendants' highly capable trial counsel, the obvious inference is that they were satisfied that they had received the essence of what they had requested on this issue. Only now, after a conviction, do they suddenly find this supposed insufficiency which they now label "plain error". The Government submits that experienced counsel may not in such circumstances escape the clear mandate of Rule 30 of the Federal Rules of Criminal Procedure. *United States* v. *Pinto*, *supra*.

F. "Unanimity"

Natelli argues (at II-F of his brief) that the Court erred in not explicitly charging that the jury must be unanimous as to the particular specification of falsity in the indictment. However, Natelli concedes that Judge

Tyler instructed the jury that they had to find, beyond a reasonable doubt, that the proxy statement was false in either one of the two specified respects in order to convict (Tr. 2340) and that their verdict had to be unanimous (Tr. 2380). The plain meaning of these instructions required unanimity on the specification of falsity; more would be unnecessary surplusage. *United States* v. *Friedman*, 445 F.2d 1076, 1083-1084 (9th Cir.), *cert. denied*, 404 U.S. 958 (1971); *Vitello* v. *United States*, 425 F.2d 416, 422-423 (9th Cir.), *cert. denied*, 400 U.S. 822 (1970). See also *United States* v. *Cook*, 497 F.2d 753, 759 (9th Cir. 1972); *United States* v. *Edwards*, 443 F.2d 1286, 1291-1292 (8th Cir.), *cert. denied*, 404 U.S. 944 (1971). Cf. *United States* v. *Papadakis*, *supra*, slip op. at 1248-1249.* The charge Judge Tyler gave on unanimity was the same as that given in *Simon* and in innumerable other cases.

G. Theory of Motive

Judge Tyler, in summarizing the Government's contentions, stated:

> ". . . [T]he Government argues that the defendants were well aware that PMM and their own local office of PMM had acquired what looked like a very promising retainer, that of NSMC, and that this retainer looked like it would be an important and perhaps profitable one, and that the defendants were well aware that they were performing a substantial role for their own firm in servicing this retainer and that they were very anxious to assist manage-

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* *Andres* v. *United States*, 333 U.S. 740 (1948), cited by appellants, simply held that in that rare situation where the final verdict is a determination, not only of guilt (there, murder) but also of punishment (there, death), the jurors who render the single verdict must be unanimous both as to guilt and as to punishment.

> ment, even to the point of aiding and abetting management in filing false earnings figures with the Securities and Exchange Commission." (Tr. 2372-3)

Natelli claims (at II-G of his brief) that there was no such evidence and the Government made no such claim. However, the Government did make that argument in summation, the defendants never objected to it, and the evidence supported it.

Thus, at Tr. 2265, Government counsel, answering an argument by Natelli's counsel, told the jury:

> A perfect smoke screen was one that you heard about at length, yesterday I believe from Mr. Martin. He was trying to tell you how Peat, Marwick & Mitchell had been very tough on National Student Marketing, so tough, in fact, it wouldn't let them have earnings when they wanted earnings, and so on, so tough that in May and in July the finance committee of National Student Marketing met and said, "Maybe we ought to fire the auditors, they are not acting aggressive enough."
>
> What does that prove after all? Just think about it. The fact is National Student Marketing was a company in a lot of trouble. They had been juggling the books, as you have seen. They had been performing frauds on everybody. They had no real sales or earnings. They needed aggressive accounting and when it came to the pinch they got it because after the May meeting and after the July meeting these two defendants went to bat for that company and put out that fraudulent proxy statement, pulled them out of a hole, allowed them to acquire four more companies.

The defense did not object to this argument. Nor could they have as it fairly stated the evidence. The evidence showed that NSMC, having already parted (as defendants knew) from one major accounting firm (Arthur Andersen), had repeatedly canvassed the question of whether to fire the auditors. (Tr. 397-401; SXE; Tr. 512). However, NSMC did not fire PMM. Following the NSMC meetings on whether to fire the auditors, Natelli and Scansaroli prepared false financial statements and thus permitted NSMC to make the acquisitions necessary to create the look of profitability. In addition, there was ample evidence of the defendants' permissiveness in allowing unbilled receivables to be booked whenever profit was needed for periods which had already closed—as post period adjustment at year end 1968, and as part of the six month and ninth month earnings reports for 1969. Further, Natelli had stated that he would allow the $1.7 million of 1968 "sales" to be booked because otherwise it might "kill the company" (Tr. 181-2); and later, at a meeting discussing NSMC's booking procedures, Randell had stated to the Finance Committee in Natelli's presence that "Tony doesn't want to see the company stabbed." (GX 16). This evidence permitted the inference which the Government drew for the jury—that of auditors abandoning their independence to please (and keep) a valued client. The Court's charge did no more than repeat for the jury the Government's contention, and was in no way in error. And even if Judge Tyler had misascribed the Government's contentions in this regard, the Court's statement would certainly not have exceeded the unquestioned authority of District Judges to comment on the evidence.

H. Aiding and Abetting

Scansaroli argues that the District Court committed error by failing to specifically instruct the jury as to the definition of "aiding and abetting." Although Scansaroli now contends that a definition of "aiding and abetting" was essential, he neither requested a definition, nor did he object to any omission of a definition from the charge.* Rather, the traditional explanation of aiding and abetting was requested and an examination of the charge to the jury demonstrates the District Court gave this instruction.

Scansaroli requested that aiding and abetting be charged, first, by a reading of 18 U.S.C. § 2.** Although the charge to the jury did not include a verbatim reading of the statute, the District Court fully covered this ground by charging that the defendant could be convicted if he made the misstatements, aided and abetted in making them, partici-

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* Defendant Scansaroli's objection to the charge was as follows: "Your Honor, I don't believe that at any point in the charge you advised the jury with respect to the aiding and abetting statute—" (Tr. 2387). Since this objection did not state "distinctly" the error now assigned on appeal, (namely, a failure to define "aiding and abetting"), Scansaroli must demonstrate that any such failure constituted plain error. F.R. Crim. P. 30, 52(b). *United States* v. *Famulari*, 447 F.2d 1377, 1382 (2d Cir. 1971).

** The criminal prohibition against aiding and abetting provides as follows:

> "(a) Whoever commits an offense against the United States or aids, abets, counsels, commands, induces or procures its commission, is punishable as a principal;
>
> (b) Whoever willfully causes an act to be done which if directly performed by him or another would be an offense against the United States, is punishable as a principal." 18 U.S.C. § 2.

pated in making them, or caused them to be made.* Had the language of the statute been charged instead, the additional words "counsels, commands, induces or procures" would have been recited. However, it is doubtful that the concept of aiding and abetting would have been any better explicated than it was by use of the common terms "participated" and "caused".**

Aside from the reading of the statute, Scansaroli sought an explanation that aiding and abetting requires the defendant to associate himself with and to participate in the venture "as in something that he wishes to bring about".*** This traditional charge was fully delivered to the jury in the following terms:

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* To this effect, the following charge was read:

"On the other hand, if you were to determine that in either or both respects the financial information or data or figures were in fact false and misleading in a material sense, then you would be obliged to consider whether or not defendants knowingly participated in making these figures and putting them in the proxy statement to be filed with the SEC, and if you did find that they either knowingly made these misstatements or they caused them to be made or they aided and abetted in their making, then you would be obliged to convict the defendant or defendants for which you make these findings." (Tr. 2341).

** A charge on aiding and abetting consisting only of a reading of the statute is sufficient. *United States* v. *Malfi*, 264 F.2d 147, 151-52 (2d Cir.), *cert. denied*, 361 U.S. 817 (1959). A charge consisting of language less complete than 18 U.S.C. § 2 is also proper. *Barsky* v. *United States*, 167 F.2d 241, 252 (D.C. Cir.), *cert. denied*, 334 U.S. 843 (1948) (approving as sufficient charge: "If one person aids or abets, advises, or counsels or encourages another to commit an offense, he is equally liable under the criminal law with one who physically commits it").

*** The defendant requested the following instruction:

"'In order to aid and abet another to commit a crime it is necessary that a defendant "in some sort associate himself with the venture, that he participate in it as in something that he wishes to bring about, that he seeks

[Footnote continued on following page]

> If you find that such a scheme has been proved and if you determine that there is some evidence that a given defendant participated in this you still have to ascertain, of course, that the prosecution has established beyond a reasonable doubt that the defendant under consideration knowingly and wilfully either put or caused to be put false or misleading material facts into that proxy statement or knowingly and wilfully assisted in this conduct with a realization of what was going on and a desire to participate in this scheme. (Tr. 2371)

At an earlier point the jury was charged that "[m]ere association, of course, is no proof of any guilty conduct whatsoever. . ." (Tr. 2336). Thus, the Court charged that Scansaroli could be convicted if he knowingly and wilfully assisted in the scheme, but the jury was warned that mere association was insufficient. As the District Court noted when defendant Scansaroli took exception, the aiding and abetting charge that he had requested was in fact given in substance.* (Tr. 2387)

In contending that "aiding and abetting" was inadequately defined, defendant relies on *United States* v. *Gar-*

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by his action to make it succeed.' " Scansaroli's Requests to Charge, No. 17, quoting from *Nye & Nissen* v. *United States*, 336 U.S. 613, 619 (1949) and *United States* v. *Peoni*, 100 F.2d 401, 402 (2d Cir. 1938).

* The District Court further noted that the summary reference and explanation of aiding and abetting was more to the Government's disadvantage than to the defendant's. (Tr. 2387). In explaining the charge and the elements of the crime, the jury was primarily charged as though they would have to find the defendant guilty as a principal in order to convict. (Tr. 2339, 2340, 2361). In a similar case, this Court stated that the District Court's failure to charge aiding and abetting was favorable rather than harmful to the defendant. *United States* v. *Colasurdo*, 453 F.2d 585, 595 n.8 (2d Cir. 1971), *cert. denied*, 406 U.S. 917 (1972).

guilo, 310 F.2d 249 (2d Cir. 1962) and *United States* v. *Terrell,* 474 F.2d 872 (2d Cir. 1973). These cases are entirely inapposite. In *Garguilo* this Court held that a defendant who was merely present during criminal acts may be entitled to a charge that mere presence and guilty knowledge are insufficient to show aiding and abetting. 310 F.2d at 254. In *Terrell,* where again the evidence amounted to mere presence and where the *Garguilo* charge was specifically requested, refusal to give it was held to be error. 474 F.2d at 876. In this case, however, neither the Government's proof nor Scansaroli's defense suggests that the defendant was a silent bystander.* Where the evidence does not reflect mere presence, a *Garguilo* charge need not be given. *McDonnell* v. *United States,* 472 F.2d 1153 (8th Cir.), *cert. denied,* 412 U.S. 942 (1973); *United States* v. *Milby,* 400 F.2d 702, 707 (6th Cir. 1968); *Loux* v. *United States,* 389 F.2d 911, 921 (9th Cir.), *cert. denied,* 393 U.S. 867 (1968). In any event, in this case the *Garguilo* charge was not requested; appellant did not object to any failure to give it; and the Court's instruction that "[m]ere association, of course, is no proof of any guilty conduct whatsoever . . ." is in fact, substantially the *Garguilo-Terrell* instruction as adapted to the facts of this case.**

Finally, although the District Court adequately instructed the jury on aiding and abetting, in this case it need not have charged aiding and abetting as a separate matter

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* In summation, Scansaroli's attorney argued that his client may have been negligent, but that he acted in good faith. (Tr. 2216-17, 2231, 2261-61a). A claim of mere physical presence was not made.

** Somewhat inexplicably, defendant also relies on *United States* v. *Byrd,* 352 F.2d 570 (2d Cir. 1965) for the proposition that the claimed failure to define "aiding and abetting" was reversible error. In *Byrd* this Court held that an omission of an instruction on criminal intent was plain error. As to aiding and abetting, the *Byrd* decision criticized the practice of reading only the statute, but held that such a charge would not constitute plain error. 352 F.2d at 576.

at all. Defendant was convicted under 15 U.S.C. § 78ff, which provides for criminal sanctions against any person who "willfully and knowingly makes or causes to be made" false and misleading statements as prohibited by the Securities Exchange Act. Where the statute itself prohibits the causing of the crime, aiding and abetting need not be additionally and specifically charged. *United States* v. *Colasurdo*, 453 F.2d 585, 595 (2d Cir. 1971), *cert. denied*, 406 U.S. 917 (1972); *cf. United States* v. *Berlin*, 472 F.2d 1002, 1009 (2d Cir.), *cert. denied*, 412 U.S. 949 (1973).

POINT III

Declaration of criminal co-venturers were properly received in evidence.

Scansaroli argues that his conviction should be reversed because six out-of-court declarations were received in evidence. Scansaroli premises his entire argument on the assertion that Judge Tyler neglected to rule that there was sufficient connection between the declarants and the defendant.* The argument is frivolous as it overlooks the Court's ruling, made at the close of the Government's case, that there was sufficient connection (Tr. 1338).** Judge Tyler spelled out this ruling more particularly as follows:

> ". . . my view is that [these objected-to declarations] are clearly admissible because count 2 really charges a scheme, as I would put it, or as the Government would put it, obviously, that what was

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* Scansaroli does not challenge the long settled rule that hearsay declarations by criminal co-venturers are admissible absent an allegation of conspiracy. *United States* v. *Annunziato*, 293 F.2d 373, 378-81 (2d Cir.), *cert. denied*, 368 U.S. 919 (1961).

** The quotation at p. 43 of Scansaroli's brief reflects Judge Tyler's views at an earlier point in the trial with respect to the Government's offer of a summary chart based upon accounting documents.

> going on here is that management decided to insist on presenting a fraudulent picture through its proxy statement in order to support its program of aggressive acquisition of other companies, mergers and the like, and then finally the management tips overboard the good sense and judgment of the defendants or one of them here and that the defendants according to the Government's theory further aided and abetted in this scheme which was primarily in the first instance at least management dominated." (Tr. 1339-40).

In addition, wholly apart from this entirely correct, e.g., *United States* v. *Zane*, 495 F.2d 683, 692 (2d Cir.), *cert. denied*, 95 S. Ct. 174 (1974), and dispositive ruling, Scansaroli's point is without substance. Since Natelli and Kurek were the only persons present at the June 3, 1969 meeting, and since both testified and were available for cross-examination, the defendant was not prejudiced even if Judge Tyler's ruling was wrong. *United States* v. *Manfredonia*, 414 F.2d 760, 765 (2d Cir. 1969); *United States* v. *Holtzman*, 440 F.2d 923, 926 (7th Cir. 1971). *Cf. United States* v. *Zane*, *supra*, 495 F.2d at 694. Scansaroli did not cross-examine either one of them with respect to this conversation. Further, Scansaroli's counsel did not even object at trial to the testimony concerning two other meetings now complained of, those of March 1, 1969 (Tr. 219) and June 9, 1969 (Tr. 243).

Finally, Scansaroli's counsel in effect conceded the lack of importance of all of the declarations now complained of by failing to ask Natelli, who was an out of court declarant at three of these conversations, a single question about these statements when Natelli took the stand. Similarly, counsel did not probe Kurek, who was present at all six meetings, with respect to his version of any of these conversations.

POINT IV

Lie detector evidence was properly excluded by the District Court.

Defendant Natelli urges that the District Court erroneously excluded results of lie detector tests proferred on the issue of intent. In assigning error to this ruling, Natelli asks this Court to upset the long-standing precedent of *Frye* v. *United States*, 293 F. 1013 (D.C. Cir. 1923), holding that polygraph evidence is inadmissible in federal criminal trials. A departure from this well-settled rule excluding polygraph evidence is entirely unwarranted.

The exclusion of the results of lie detector test has been upheld by this Circuit and by every other Circuit that has considered the question. *United States ex rel. Sadowy* v. *Fay*, 284 F.2d 426 (2d Cir.), *cert. denied*, 365 U.S. 850 (1960); *United States* v. *Cochran*, 499 F.2d 380, 393 (5th Cir. 1974); *United States* v. *Gloria*, 494 F.2d 477, 483 (5th Cir. 1974); *United States* v. *Pacheo*, 489 F.2d 554, 566 (5th Cir. 1974); *United States* v. *Frogge*, 476 F.2d 969, 970 (5th Cir.), *cert. denied*, 414 U.S. 849 (1973); *United States* v. *Noel*, 490 F.2d 89, 90 (6th Cir. 1974); *United States* v. *Tremont*, 351 F.2d 144, 146 (6th Cir. 1965), *cert. denied*, 383 U.S. 944 (1966); *United States* v. *Chastain*, 435 F.2d 686, 687 (7th Cir. 1970); *United States* v. *Penick*, 496 F.2d 1105, 1109 (7th Cir. 1974); *United States* v. *Sockel*, 478 F.2d 1134, 1135 (8th Cir. 1973); *Mc Croskey* v. *United States*, 339 F.2d 895 (8th Cir. 1965); *United States* v. *Alvarez*, 472 F.2d 111, 113 (9th Cir.), *cert. denied*, 412 U.S. 921 (1973); *United States* v. *De Betham*, 470 F.2d 1367, 1368 (9th Cir. 1972), *cert. denied*, 412 U.S. 907 (1973); *United States* v. *Jenkins*, 470 F.2d 1061, 1064 (9th Cir. 1972), *cert. denied*, 411 U.S. 920 (1973); *United States* v. *Salazar-Goeta*, 447 F.2d 468, 469 (9th Cir. 1971); *United States* v. *Sadrzadeh*, 440 F.2d 389, 390 (9th Cir.),

cert. denied, 404 U.S. 850 (1971); *United States* v. *Rodgers,* 419 F.2d 1315, 1319 (10th Cir. 1969); *United States* v. *Wainwright,* 413 F.2d 796, 802 (10th Cir. 1969), *cert. denied,* 396 U.S. 1009 (1970); *Marks* v. *United States,* 260 F.2d 377, 382 (10th Cir. 1958), *cert. denied,* 358 U.S. 929 (1959); *United States* v. *Skeens,* 494 F.2d 1050, 1053 (D.C. Cir. 1974); *United States* v. *Zeiger,* 475 F.2d 1280 (D.C. Cir. 1972).*

The lower court cases which support admissibility, *United States* v. *Ridling,* 350 F. Supp. 90 (E.D. Mich. 1972) and *United States* v. *Zeiger,* 350 F. Supp. 685 (D.D.C.), *rev'd,* 475 F.2d 1280 (D.C. Cir. 1972) are aberrational. District Courts considering the question have generally followed the well-settled rule and excluded polygraph evidence. *See, e.g., United States* v. *Wilson,* 361 F. Supp. 510 (D. Md. 1973); *United States* v. *Levinson,* 369 F. Supp. 575 (E.D. Mich. 1973); *United States* v. *Stromberg,* 179 F. Supp. 278 (S.D.N.Y. 1959).

The continued vigor of the rule excluding polygraph evidence is due to the strength of its underlying rationale. As courts considering the issues have noted, the danger of the polygraph is that, with its aura of scientific infallibility, too much weight will be attached to its purported ability to detect the truth. *See Frye* v. *United States, supra.* Whatever the improvements in the polygraph since *Frye,* it con-

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* Natelli cites *United States* v. *Wainwright, supra,* in support of the admissibility of polygraph evidence (Natelli Br. at 83). However, despite *dicta* in that case favorable to defendant's position, in a subsequent decision the Tenth Circuit cited *Wainwright* in stating that "[w]e have held that results of a lie detector test are inadmissible." *United States* v. *Rodgers,* 419 F.2d 1315, 1319 (10th Cir. 1969). Likewise, although defendant cites Fifth Circuit cases in support of his contention, (Natelli Br. at 83), in *United States* v. *Cochran,* 499 F.2d 380, 393 (5th Cir. 1974) the Fifth Circuit flatly stated that it is well-established that lie detector tests are inadmissible.

tinued fallibility could entirely subvert the trial process if evidence based on it were to be admitted.

Furthermore, the wisdom of the rule is well-illustrated in this case where the opinion of the polygraph operator was claimed to show that defendants were telling the truth with respect to the question posed by the polygraph operator, but the evidence before the jury was quite to the contrary. On cross-examination it was proved that the defendants' testimony at trial was inconsistent with prior sworn testimony and with documents prepared at the time of the events in issue. (*Supra* at 20; 32; 42). Based on this, and, of course, on demeanor evidence, the jury in this case found that these defendants lied.* The Government submits that the jury's determination, based on all of the evidence in the case remains a more trustworthy basis for determining the truth than the results of the polygraph.

Thus, both the weight of precedent and reason support the District Court's determination that polygraph evidence was inadmissible. In any event, even under the cases cited by defendant as most favorable to him, this would be a matter within the discretion of the trial court, and the exclusion of polygraph evidence has never been held to be an abuse discretion. *See United States* v. *Penick, supra; United States* v. *Chastain, supra; United States* v. *De Betham, supra.*

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* As both defendants told the jury they did not intend to mislead, and as the Government told the jury, "if you can't believe them, you must convict them" (Tr. 2314), the issue was squarely put.

POINT V

There was no adverse publicity warranting dismissal of the indictment.

Natelli claims that the indictment should be dismissed because of "deliberate misconduct of a senior Government official involved in this prosecution." (Natelli Br. at 84). The facts show that there was no misconduct and no effect whatever on the jury. Accordingly, there is no basis for dismissing the indictment.

a) There was no misconduct.

Claiming that this is a case of "deliberate misconduct", Natelli quotes a line buried in a long article published in the Wall Street Journal on October 29, 1974. The reporter quoted "a Washington source" as saying "if we can't get a conviction here, we never will." After the article was brought to the Court's attention at trial the Government ascertained that the Washington source was John C. Burton, Chief Accountant with the Securities & Exchange Commission. In a signed memorandum presented to the District Court, Mr. Burton explained that on October 11, 1974, he had lunch with Frederick Andrews, who was the author of the *Journal* article and a personal friend of Mr. Burton's. During the luncheon, while discussing general SEC matters, Mr. Burton had stated "if we can't convince a jury in this case, we will have to rethink the whole question of criminal references." * As he represented to the District Court in

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* The context of this statement shows that Burton was referring to the relative *simplicity* of this case as compared with Four Seasons, and was in no way referring to the merits of the case or commenting on the defendants' "guilt or innocence." Thus, Mr. Burton stated: "Since Mr. Andrews had read the transcripts of the Four Seasons trial, we discussed that briefly and I indicated my judgment that the National Student Marketing Case was fundamentally much simpler. *It was in this connection* that I said something like "if we can't convince a jury in this case, we will have to rethink the whole question of criminal references." (Ct. X 2)

his memorandum, Mr. Burton believed this statement to recount more accurately his words to the reporter than did the quote attributed to him in the article. Thus, whatever the implication of the quote in the *Journal* article, the statement made by Mr. Burton did not amount to any opinion by him that the defendants were guilty.

Nor was the statement given under circumstances indicating a desire to affect the trial. This was not a press release or a press conference, but a comment at an informal lunch with a personal friend. Therefore, contrary to defendant's characterization of the incident, there was no deliberate misconduct involved. *United States* v. *Grassia*, 354 F.2d 27, 29 (2d Cir. 1965), *vacated on other grounds*, 390 U.S. 202 (1968), relied upon by defendant, suggests that dismissal of an indictment may be warranted where the Government generates publicity. However, it does not apply to this case where Mr. Burton's actions could not fairly be labelled "misconduct". Contrast *United States* v. *Capra*, 501 F.2d 267, 277-279 (2d Cir. 1974), *cert. denied*, 43 U.S.L.W. 3515 (March 24, 1975); *United States* v. *Abbott Laboratories, Inc.*, 505 F.2d 565, 568-572 (4th Cir. 1974), *cert. denied*, 43 U.S.L.W. 3515 (March 24, 1975).

b) The Court acted properly in questioning the Jurors, at the request of defendants, in the absence of counsel; Natelli's claim that the Court might have done more was expressly waived.

Natelli argues that dismissal may be required because the jury was possibly prejudiced by the statement contained in the *Journal* article. This contention is unfair and an imposition on the Court.

Defendants studiously avoided moving for a mistrial on this issue. (Tr. Nov. 6 at 2; Nov. 7 at 15). Both below and here on appeal, they have contended only that the indictment should be dismissed. In so doing, they have clearly

waived any claim to a retrial before a new and presumably uninfected jury.

Moreover, the record below clearly reflects that the jury that convicted Natelli and Scansaroli had no knowledge of the *Journal* article and therefore could not be prejudiced against them as a result of it. E.g., *United States* v. *Noah*, 475 F.2d 688, 692-693 (9th Cir. 1973). However, most important, when the publication of the *Wall Street Journal* article was brought to the District Court's attention, each juror was individually questioned by the Court about his knowledge of it. Each juror told the District Court Judge that he had not read or heard the contents of the article. (Tr. Nov. 7 at 4-13). After personally questioning each juror, Judge Tyler stated that he "did not see or observe or feel anything that led me to disbelieve any of these people." (Tr. Nov. 7 at 14).

As to any claim that the District Court's questioning of the jury was insufficient, it was Mr. Martin, counsel for Natelli below and on this appeal, who requested that "the Court in the absence of counsel, speak to each juror . . ." The Court responded: "I prefer that you listen to this." Mr. Martin declined, stating that "it might be less imposing for jurors involved to have it just with the Court." (Tr. Nov. 6 at 2). Counsel now seeks to avoid the facts as the District Court found them. Thus, he argues that, as to particular jurors, the District Court did not "inquire further," and speculates that such inquiries might have produced evidence of taint. (Natelli Br. at 86). However, having specifically declined to be present at the voir dire, it is plainly unfair to urge here that the District Court's determination was incomplete or improperly handled.

The District Court denied the motion to dismiss on the ground that the jury knew nothing of the newspaper story (Tr. 2434), and this ruling was in total accordance with the pertinent law. The governing standard was recently

stated by this Court in *United States* v. *Capra, supra,* 501 F.2d at 279:

> "Absent proof of bias on the part of individual members of a jury, reversal, because of extensive publicity adverse to the accused, is required where, after reading or hearing it, a resulting conclusion of guilt in the minds of the general public would be practically certain . . . or where improper pressure on a jury was clear from the record itself. . . .

The standard set forth in *Capra* was not met in this case. The adverse publicity was not "extensive." The article could not possibly have led to "a resulting conclusion of guilt in the minds of the general public," nor does defendant claim that it did. Finally, the voir dire of the jury insured that there was no knowledge and, accordingly, no chance of any "improper pressure" on the jury because of the article. In fact, the District Court was "not at all convinced that the so-called offending article is really unfavorable to the defense" (Tr. Nov. 7 at 3), and, thus, it is unclear that the article even if known to the jury, would have created any "pressure" against the defendant at all.

However, even if some small negative effect were possible, far more substantial intrusions of publicity than occurred in this case have been held not to constitute a violation of a defendant's rights. *E.g., United States* v. *Manfredi,* 488 F.2d 588, 603-604 (2d Cir. 1973), *cert. denied,* 417 U.S. 936 (1974); *United States* v. *Pfingst,* 477 F.2d 177, 184-186 (2d Cir.), *cert. denied,* 412 U.S. 941 (1973); *United States* v. *Palmieri,* 456 F.2d 9, 13-14 (2d Cir.), *cert. denied,* 406 U.S. 945 (1972); *Margoles* v. *United States,* 407 F.2d 727, 728-735 (7th Cir.), *cert. denied,* 396 U.S. 833 (1969). Accordingly, here where the publicity was minimal and the jury untainted, the District Court properly denied the motion to dismiss.

c) Natelli is not entitled to any relief in view of extensive publicity inspired by the defense.

Natelli (Br. at 89) cites *dicta* in which this Court spoke of the possibility that the drastic sanction of dismissal of an indictment may be warranted by "the Government's conduct in generating publicity . . ." *Untied States* v. *Grassia*, 354 F.2d 27, 29 (2d Cir. 1965), *vacated on other grounds*, 390 U.S. 202 (1968). However, the rationale for imposing such sanctions on the Government, even where arguably appropriate, should plainly be obviated by the instigation by the defendant of prejudicial publicity. In this case, defendants' accounting firm, Peat Marwick & Mitchell, from the day of indictment through the day of sentencing, conducted a publicity campaign which surely reduced any passing comment by Mr. Burton to an inaudible whisper.*

In view of the circumstances surrounding Mr. Burton's offhand comment, the fact that the jurors were unaware of the article, and the defendants' publicity campaign, the District Court's ruling on this issue should not be disturbed.

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* After the filing of the indictment in this case, the defendants' firm, which, according to the affidavit of William Hegarty (*amicus* brief for PMM at 2a) has "aided both Mr. Natelli and Mr. Scansaroli throughout in their defense", issued a press release expressing their confidence in the defendants' denials of guilt and claiming that Scansaroli had "passed" a polygraph test. This release was followed by a 14-page statement on the pending case, including a claim that "the Grand Jury process fails to protect innocent individuals." And, as noted by the District Court at sentencing (Tr. 12/27/74 at 11), the guilty verdict was followed by a press release claiming that the convictions were the result of confusion on the part of the jury.

POINT VI

Venue was proper in the Southern District of New York.

Natelli argues that the indictment should be dismissed, claiming that venue for a charge under Section 32 of the Securities Exchange Act, 15 U.S.C. § 78ff, could not properly be laid in the Southern District of New York. At trial, the Government proved that defendants Natelli and Scansaroli actually prepared both the false footnote and the false nine month earnings statement at the Pandick Press in Manhattan (Tr. 250 *et seq.;* 651 *et seq.;* 2059-2061.) Natelli contends that the preparation of false proxy material in the Southern District of New York does not constitute a proper basis for venue because an offense under § 78ff may only be prosecuted in the district in which the false statement was filed, that is, Washington.* This narrow view of venue is unsupported in precedent or reason.

The statute under which defendant was charged provides in pertinent part as follows:

> Any person who willfully and knowingly makes, or causes to be made, any statement in any application, report or document required to be filed under this chapter or any rule or regulation thereunder . . . [shall be guilty of a crime]. 15 U.S.C. § 78ff.**

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* While Natelli and Scansaroli challenged venue in his pre-trial motions, neither defendant moved for a change of venue to Washington, D.C., as did the defendants Randell and Davies.

** The Government contended below and the District Court found in its decision on the pre-trial venue motion that the gravamen of the violation under 15 U.S.C. § 78ff was the making of the false statement, not the filing, as defendant contends. Thus, in denying the motion in which defendant contended that that venue must be laid in the district of filing, the Court held that the words of the statute, "required to be filed," merely de-

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scribed a category of documents rather than the essence of the offense.

Much of Natelli's venue argument appears to hinge on the assertion in his brief (at 92) that the offense charged only occurred when the false proxy statement was filed with the SEC in Washington. From this he concludes that venue was only proper there.

Assuming *arguendo* that Natelli is correct that the offense charged is only completed upon the presentation of the false proxy statement to the SEC in Washington, it by no means follows that venue lies only in the District of Columbia. See *United States* v. *Bithoney*, 472 F.2d 16, 21-25 (2d Cir.), *cert. denied*, 412 U.S. 938 (1973). In *Bithoney* this Court was presented with the converse of the claim raised here. The defendants had been convicted of making a false acknowledgement on an immigration document (18 U.S.C. § 1015(d)) later filed with the Immigration and Naturalization Service in Buffalo. The defendants claimed that since the false attestation forbidden by the statute had been made by them in Boston, their prosecution in the Western District of New York, rather than in Boston, violated the venue provisions of the Sixth Amendment. This Court held that since the offense charged was not completed until the false document was submitted in Buffalo, venue there was proper.

In reaching that conclusion, this Court relied on *United States* v. *Newton*, 68 F. Supp. 952 (W.D. Va. 1946), *aff'd*, 162 F.2d 795 (4th Cir. 1947), *cert. denied*, 333 U.S. 848 (1948). In *Newton*, the defendant had prepared a fraudulent income tax return in the Western District of Virginia and filed it in the Eastern District of Virginia. The District Court agreed that the offense was not completed until the filing of the return in the Eastern District but rejected the claim that venue did not lie in the Western District. Judge Medina's discussion of *Newton* *in Bithoney*, 472 F.2d at 23-23, is instructive here:

> "The Fourth Circuit strongly intimated that in effect this was a crime committed in two districts and venue would lie in either one. . . Thus, assuming that the filing of the claim was an essential element of the crime charged, the court in *Newton* still held that venue was proper in the district where the crime began. [Further citations omitted]
>
> Of course, in *Newton* the defendant presented the opposite side of the argument from that proffered by the

[Footnote continued on following page]

The venue provision for offenses under the Securities Exchange Act authorizes a trial in "the district wherein any act or transaction constituting the violation occurred." 15 U.S.C. § 78aa. This broad provision is supplemented by the general venue provision for continuing offenses:

> "Except as otherwise expressly provided by enactment of Congress any offense against the United States begun in one district and completed in another, or committed in more than one district, may be inquired of and prosecuted in any district in which such offense was begun, continued, or completed." 18 U.S.C. § 3237(a).

Apart from the question of whether venue could be upheld under the broad provisions of 15 U.S.C. § 78aa alone, venue was proper in this case under 18 U.S.C. § 3237(a). This Court held in *United States* v. *Cashin*, 281 F.2d 669, 673 (2d Cir. 1960), that venue for a false filing offense, substantially identical to the one in this case, could properly be found under 18 U.S.C. § 3237(a). In that case the false statements were filed in Washington, but this Court found venue in Alabama to be proper. Likewise, in *United States* v. *Pope*, 189 F. Supp. 12 (S.D.N.Y. 1960), where again there was a false filing charge identical to Count Two in this case, Judge Weinfeld held that venue was proper in the Southern District of New York under the provisions of 18 U.S.C. § 3237. Most recently, this Court denied a petition for mandamus where an indictment containing false filing counts was transferred for trial from the Southern District of New York, where the filing had been made, to

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appellants in this case. However, the decision certainly supports our view that a crime is not complete until the false document . . . is actually used by the participants by filing it . . . The crime is begun in one district, and venue may be proper there, but it is completed in another district where venue most definitedly lies. We are not required to decide if venue would have been proper in Massachusetts."

the Western District of Oklahoma, where the statements had been prepared. *United States* v. *Clark*, 360 F. Supp. 936 (S.D.N.Y.), *mandamus denied sub. nom. United States* v. *Griesa*, 481 F.2d 276 (2d Cir. 1973). In holding that it was not an abuse of discretion to transfer the case to Oklahoma for trial, this Court implicitly found that venue on the false filing counts could properly be laid outside this district where the filing had occurred.*

In the face of these precedents** Natelli hinges his venue argument essentially on a Supreme Court decision of limited scope. That case, *United States* v. *Travis*, 364 U.S. 631 (1961), held that the proper venue for offenses under 18 U.S.C. § 1001, the False Statements Act, is in the district in which the false statement was made. In pressing the importance of this decision, Natelli fails to note that *Travis* has never been applied to a false filing offense under the securities laws. Indeed, this Court has limited the *Travis* decision to its peculiar facts. In *United States* v. *Slutsky*, 487 F.2d 832 (2d Cir. 1973), *cert. denied*, 416 U.S. 937 (1974), this Court, through Judge Timbers, distinguished the *Travis* case and held venue to be proper in the Southern District of New York where tax returns had been prepared, although the returns were required to be filed in the Northern District:

> "[T]he law in this Circuit is settled that venue properly lies where a false statement is prepared and signed, even though received and filed elsewhere, by

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* The issue in that case was focussed by the dissent of Judge Timbers, quoted at pp. 92-93 of Natelli's brief.

** *See also*, as to decisions of this Circuit, *United States* v. *Gross*, 276 F.2d 816 (2d Cir.), *cert. denied*, 363 U.S. 831 (1960); *United States* v. *Miller*, 246 F.2d 486 (2d Cir.), *cert. denied*, 355 U.S. 905 (1957); *United States* v. *Bithoney*, *supra*. As to other circuits *see United States* v. *Henslee*, 262 F.2d 750 (5th Cir.), *cert. denied*, 359 U.S. 984 (1959); *Newton* v. *United States*, *supra*. *But see United States* v. *Valenti*, 207 F.2d 242 (3rd C.R. 1953); *Reass* v. *United States*, 99 F.2d 752 (4th Cir. 1938).

operation of the 'continuing offense' statute." 487 F.2d at 839.

"Travis v. United States, 364 U.S. 631 (1961), is not to the contrary. While that case held that the alleged violation of 18 U.S.C. § 1001 (making false statements) could be prosecuted only in the district in which the affidavit had been filed, the decision surely was meant to be confined to the facts based on the unusual statute involved." 487 F.2d at 839, n. 8.*

Moreover, in *United States* v. *Candella,* 487 F.2d 1223 (2d Cir. 1973), *cert. denied,* 415 U.S. 977 (1974), this Court held venue to be proper in a district other than the one of filing, even though that case involved a violation of 18 U.S.C. § 1001, as did *Travis.*

The Seventh and Tenth Circuit Courts of Appeal have similarly refused to extend the *Travis* decision beyond its own facts. In *Imperial Meat Co.* v. *United States,* 316 F.2d 435 (10th Cir.), *cert. denied,* 375 U.S. 820 (1963), the Tenth Circuit held that charges of false claims, in violation of 18 U.S.C. § 287, were properly tried where the false invoices were prepared but not filed. The Court brushed *Travis* aside, simply noting that "reliance by appellants on the *Travis* case is not justified." 316 F.2d at 440. In *United States* v. *Ruehrup,* 333 F.2d 641, 643 (7th Cir.), *cert. denied,* 379 U.S. 903 (1964), the Seventh Circuit held that a false statement to the Bank of Farm Credit Administration was properly tried where the statement was prepared and mailed. In so doing that Court stated "that Travis is not controlling and is limited to the statute there involved." 333 F.2d at 643.**

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* It seems clear that "the unusual statute involved" in *Travis* was not 18 U.S.C. § 1001 but rather Section 9h of the Taft-Hartley Act.

** Appellant has attempted to distinguish the *Imperial Meat Co.* and *Ruehrup* decisions by arguing that they relied on that

[Footnote continued on following page]

Finally, the weakness of Natelli's legal authority on this issue is fully matched by the infirmity of the underlying reasoning. If Natelli's position on venue were upheld, prosecutions such as this one for false filings could be tried only in Washington, D.C. even if all the acts of falsification occurred elsewhere and a messenger uninvolved with the crime delivered the documents containing the false statements to the District of Columbia for filing. This result would directly contravene the fundamental Constitutional purpose of venue, which is to ensure trial in the locality of the offense rather than in some far away district unconnected to the location of the criminal deeds. *See United States* v. *Cores*, 356 U.S. 405, 407 (1958).

In any event, even if this Court held the situs of the filing to be the proper district for venue under 15 U.S.C. § 78ff, venue in this case would nevertheless be proper. Defendants, who were tried as aiders and abettors, (as well as principals) committed accessorial acts in the Southern District of New York, which under the decisions of this Court would provide a proper basis for venue in this district.* *United States* v. *Bozza*, 365 F.2d 206 (2d Cir. 1965); *United States* v. *Gillette*, 189 F.2d 449 (2d Cir.), *cert. denied*, 342 U.S. 827 (1951); *United States* v. *Sweig*, 316 F. Supp. 1148 (S.D.N.Y. 1970); *United States* v. *Pope*, 189 F. Supp. 12 (S.D.N.Y. 1960).

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portion of § 3237(a) which grounds venue on the use of the mails, a factor not present in this case. (Natelli Br. at 95). However, this suggested distinction is entirely without foundation since neither case even refers to that portion of § 3237(a) relating to use of the mails.

* Natelli contends that he was tried as a principal (Natelli Br. at 96). However, as the charge to the jury demonstrates, the case against both defendants was submitted to the jury on the theory that they could be found to be guilty as aiders and abettors (Tr. 2341). Indeed, in his brief, Scansaroli argues that the District Court committed error by charging the jury that defendants could be found guilty as aiders and abettors without defining those terms in detail. (Scansaroli Br. at 53-57).

POINT VII

Schauer's testimony was admissible.

Defendant Scansaroli contends that the District Court erroneously permitted so-called "fraud victim" testimony to be admitted into evidence. Specifically, Scansaroli quarrels with the admission of two portions of Louis Schauer's testimony.* First, defendant assigns error to the admission of Mr. Schauer's statement that, before (INC) closed its deal with NSMC, he did not know that over $1 million of the $1.7 million of 1968 unbilled receivables, and $2 million of the $3.3 million 1968 and 1969 unbilled accounts receivables had been written off (Tr. 1058). Second, defendant objects to the admission of Mr. Schauer's testimony that the 1300 shareholders of Interstate exchanged their stock for shares in NSMC. (Tr. 1060-61). Contrary to defendant's contention, the admission of Mr. Schauer's testimony on these points was not in violation of any ruling of the District Court and, in any event, the testimony was proper and admissible.

In arguing this issue Scansaroli makes much of a claim that the testimony was admitted in violation of an earlier ruling by the District Court. Whatever the possible relevance of that argument, it completely misconstrues the District Court's ruling. In response to briefs that specifically focussed on the issue, the District Court ruled that the Government could not offer testimony as to what a victim of the fraud *would have done* if he had known the facts which were not disclosed. (Tr. 697-98, 702). The Government abided by that ruling and neither elicited nor attempted to elicit, testimony as to what any witness would

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* Scansaroli, having failed to object at trial, does not contest on appeal the admission of similar testimony given by Arthur Frommer. (Tr. 1022-23, 1031).

have done had the true facts been revealed. But when Scansaroli's attorney objected to Mr. Schauer's testimony on the ground that it was in violation of the Court's ruling, Judge Tyler stated that he disagreed. (Tr. 1059).

Apart from this reliance on the purported departure of the District Court from its own ruling, Scansaroli claims on appeal that Mr. Schauer's testimony constituted prejudicial and inflammatory "victim" evidence, offered to "arouse the jury's passion." (Scansaroli Br. at 52). However, this characterization strains the record in this case. There was no parade of victims. There was no testimony of the specific losses suffered by each victim of the fraud. Therefore, Mr. Schauer's statement of the exchange of stock did not amount to "fraud victim" evidence as discussed in the cases cited by defendant (Scansaroli Br. at 50-52). In any event, such evidence is admissible under the decisions of this Court. *United States* v. *Brown*, 79 F.2d 321 (2d Cir.), *cert. denied, sub. nom. McCarthy* v. *United States*, 296 U.S. 650 (1935); *Rice* v. *United States*, 35 F.2d 689 (2d Cir. 1929), *cert. denied*, 281 U.S. 730 (1930). *Cf. United States* v. *Minuse*, 142 F.2d 388 (2d Cir.), *cert. denied*, 323 U.S. 716 (1944); *United States* v. *Aloi*, 74-1220 (2d Cir., January 31, 1975), slip op. at 6083-6084.

Schauer's testimony was relevant and admissible to show the significance of the proxy statement generally and of the misstatements and omissions in it particularly in connection with the NSMC-INC acquisition. Schauer testified that the unbilled "sales" had been a point of interest to the INC board and that they had never been told the true facts regarding those "sales" before INC closed the transaction. (Tr. 1033-42; 1057-61). This testimony was important to forestall jury speculation regarding the information INC had prior to the closing, particularly since the jury had before it in evidence the PMM comfort letter, which corrected part, but not all, of the misstatements and

omissions in the proxy statement. The admission of the testimony was accordingly no abuse of Judge Tyler's discretion, the exercise of which cannot be disturbed on appeal except for "grave 'abuse'" hardly demonstrated here. *United States* v. *Gottlieb, supra,* 493 F.2d at 992.

CONCLUSION

The judgments of conviction should be affirmed.

Respectfully submitted,

PAUL J. CURRAN,
United States Attorney for the Southern District of New York, Attorney for the United States of America.

FRANKLIN B. VELIE,
JED S. RAKOFF,
AUDREY STRAUSS,
JOHN D. GORDAN, III,
Assistant United States Attorneys,
Of Counsel.

GX 65- 2

GX 65-11

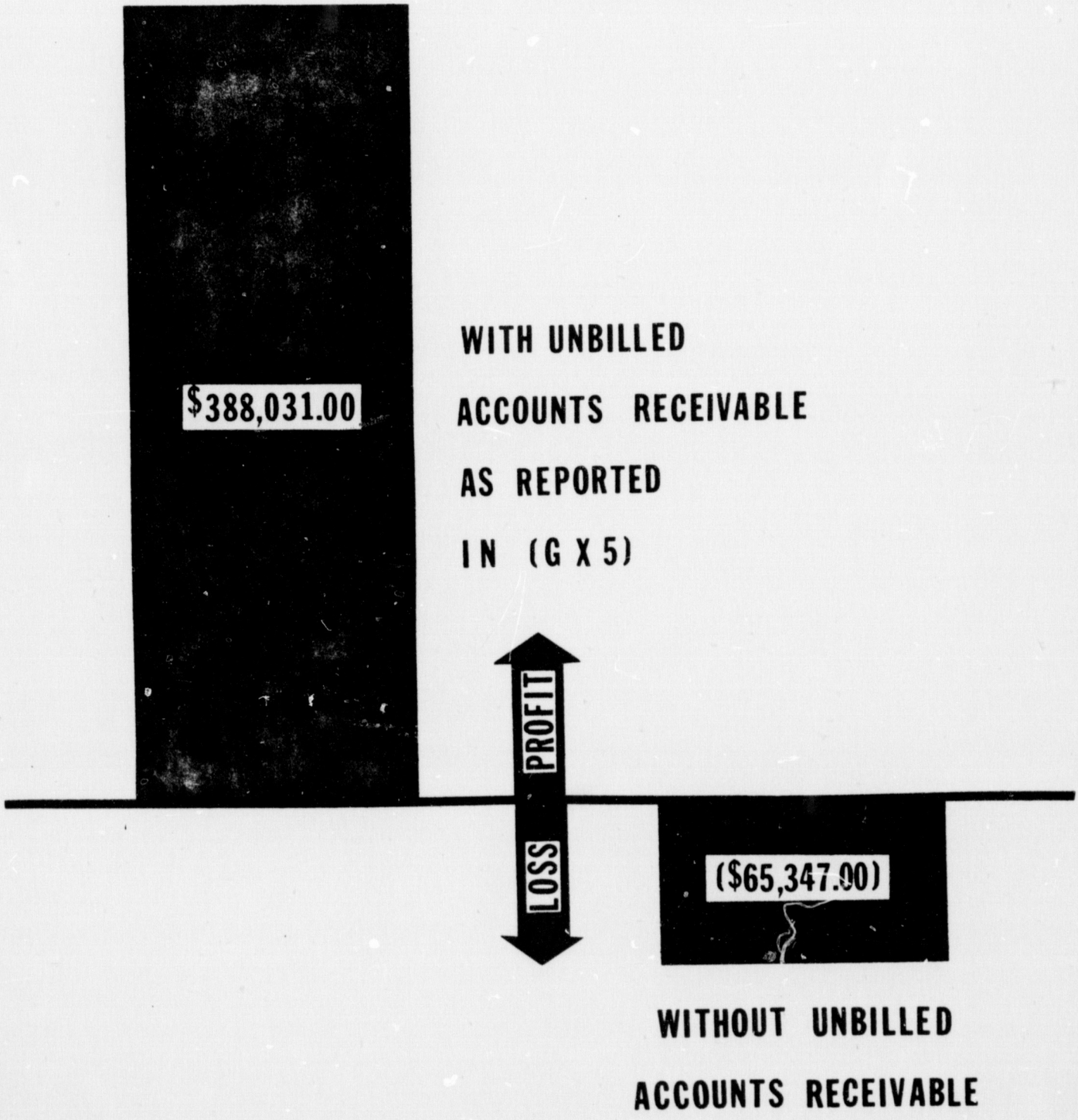
GX 65-14

GX 65-15

[For the Convenience of Court and Counsel these Exhibits are reproduced on the opposite page.]

GX 65-2

1968
N S M C CONSOLIDATED NET EARNINGS



GX 65- 11

N S M C CONSOLIDATED 1968 SALES PER NOTE D,

FINAL PROXY G x 25

(D) Net sales and earnings as originally reported to stockholders in the annual reports for the years 1967 and 1968 and original prospectus for the year 1966 and the amounts as shown in the statement of earnings in this proxy statement are reconciled as follows:

	1966	1967	1968
Net sales:			
Originally reported	$ 573,259	$2,386,500	$ 4,989,446
Pooled companies reflected retroactively	2,084,915	3,266,360	6,552,449
Per statement of earnings	$2,658,174	$5,652,860	$11,541,895

NOT DISCLOSED:

OVER $1,000,000.00 OF N S M C 1968 SALES ORIGINALLY REPORTED HAVE BEEN WRITTEN OFF.

$748,762.00 OF THESE SALES LOSSES ARE SUBTRACTED FROM POOLED COMPANIES, NOT FROM N S M C.

GX 65-14

STATUS OF 1968 AND 1ST HALF 1969 UNBILLED ACCOUNTS RECEIVABLE SALES AS OF AUGUST 18, 1969. SUMMARY OF ENTRIES IN G x 3, 13, 15

$3,347,775.00 — 100%

BILLED OR BILLED IN PART

$858,274.00 (26%)

$2,489,501.00 — 74%

INACTIVE

$123,006.00 (4%)

$2,366,495.00 — 70%

"BAD" OR "TO BE WRITTEN OFF"

$310,972.00 (9%)

$2,055,523.00 — 61%

WRITTEN OFF

$2,055,523.00 (61%)

GX 65-15

CLIENT	AMOUNT	MAY, 1969 REVIEW			AUGUST, 1969 REVIEW			COMFORT LETTER
		DATE	ACCOUNTANT	COMMENT	DATE	ACCOUNTANT	COMMENT	
BARNES - HIND	$22,400.00	5/22	J.S.	DELETE	8/15	D.H.O.	BAD	—
CAMPANA	21,900.00	5/22	J.S.	WRITE OFF	8/15	D.H.O.	BAD	•
FABERGE	53,775.00	5/22	J.S.	NO CONTRACT	8/15	D.H.O.	BAD	•
GOSSARD	53,775.00	5/22	J.S.	NO CONTRACT	8/15	D.H.O.	BAD	•
PACE	14,492.00	5/22	J.S.	WRITE OFF	—	—	—	•
CARNATION	11,200.00	5/22	J.S.	DELETE	—	—	—	—
BARNES - HIND	47,850.00	—	—	—	8/15	D.H.O.	BAD	•
BIZAAR	5,580.00	—	—	—	8/15	D.H.O.	BAD	•
EASTERN	27,000.00	—	—	—	8/15	D.H.O.	BAD	—
SCHICK	30,000.00	—	—	—	8/16	D.H.O.	DUPLICATED	•
TANYA	32,200.00	—	—	—	8/15	D.H.O.	BAD	—
SUB TOTAL	320,172.00							
EASTERN	519,152.00							
TOTAL	$ 839,324.00							

8/15 DHO BOOKED

GX 65-10

[*For the Convenience of Court and Counsel this Exhibit is printed on the opposite page.*]

★ U. S. Government Printing Office 1975— 614—213—491

NATIONAL STUDENT MARKETING CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED STATEMENT OF EARNINGS—(Concluded)

is best matched against costs directly connected with the production of this income by recording the estimated gross profit based on the percentage of time incurred to the total estimated time to be incurred by the employees in development of the over-all program for the client. Accordingly, commencing in 1968 all such programs have been accounted for on this basis upon obtaining a client commitment.

(C) [redacted]

(D) The average number of shares outstanding during each year has been adjusted: (1) for the stock split described in note 8 to the consolidated financial statements (2) to include the equivalent of the number of shares of common stock outstanding of companies acquired in [redacted] transactions accounted for as poolings of interests and (3) to give effect to exercise of all outstanding stock options.

(E) Net sales and earnings as originally reported to stockholders in the annual report for the years 1967 and 1968 and original prospectus for the year 1966 and the amounts as shown in the [redacted] of earnings in this proxy statement are reconciled as follows:

	1966	1967	1968
Net sales:			
Originally reported	$ 573,259	$2,386,500	$ 4,989,446
[redacted]			
Pooled companies reflected retroactively	2,084,915	3,266,360	[redacted]
	$2,658,174	$5,652,860	[redacted]
Net earnings (loss):			
Originally reported	(4,510)	168,616	388,031
[redacted]			
Pooled companies reflected retroactively	80,059	217,019	[redacted]
	$ 75,549	$ 385,635	$ 756,460

Figures for 1968 have been restated in certain instances to make the presentation consistent with current accounting practices. There was no material effect as a result of such restatement.

(3) Foreign study programs:

The operations of New England Travel Corporation (a wholly-owned subsidiary described elsewhere in the Proxy Statement) involve arrangements by the company of study programs abroad during the summer months for high school students. Results of operations are accounted for during the summer months as the study programs are completed and students return to the United States. Consequently, all costs are deferred during the first nine months of the year. As a result the unaudited [redacted] month figures in the consolidated statements of earnings exclude any operations of New England Travel Corporation. [redacted]

NATIONAL STUDENT MARKETING CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED STATEMENT OF EARNINGS—(Concluded)

is best matched against costs directly connected with the production of this income by recording the estimated gross profit based on the percentage of time incurred to the total estimated time to be incurred by the employees in development of the over-all program for the client. Accordingly, commencing in 1968 all such programs have been accounted for on this basis upon obtaining a client commitment.

(C) Retroactive adjustment was made in the consolidated statement of earnings for the year 1968 for certain contract losses and for recognition of effect on deferred taxes of related net operating loss carryforwards. The net effect of the retroactive adjustment was a $21,000 decrease in net earnings for the year 1968.

(D) The average number of shares outstanding during each year has been adjusted: (1) for the stock split described in note 8 to the consolidated financial statements (2) to include the equivalent of the number of shares of common stock outstanding of companies acquired in certain transactions accounted for as poolings of interests and (3) to give effect to exercise of all outstanding stock options.

(E) Net sales and earnings as originally reported to stockholders in the annual report for the years 1967 and 1968 and original prospectus for the year 1966 and the amounts as shown in the summary of earnings in this proxy statement are reconciled as follows:

	1966	1967	1968
Net sales:			
Originally reported	$ 573,259	$2,386,500	$ 4,989,446
Retroactive adjustment for contract losses (note C)	—	—	(70,200)
Pooled companies reflected retroactively	2,084,915	3,266,360	6,389,164
	$2,658,174	$5,652,860	$11,308,410
Net earnings (loss):			
Originally reported	(4,510)	168,616	388,031
Retroactive adjustment for contract losses (note C)	—	—	(21,000)
Pooled companies reflected retroactively	80,059	217,019	389,429
Per summary of earnings	$ 75,549	$ 385,635	$ 756,460

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NATIONAL STUDENT MARKETING CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED STATEMENT OF EARNINGS—(Concluded)

is best matched against costs directly connected with the production of this income by recording the estimated gross profit based on the percentage of time incurred to the total estimated time to be incurred by the employees in development of the over-all program for the client. Accordingly, commencing in 1968 all such programs have been accounted for on this basis upon obtaining a client commitment.

(3) Foreign study programs:

The operations of New England Travel Corporation (a wholly-owned subsidiary described elsewhere in the proxy statement) involve arrangements by the company of study programs abroad during the summer months for high school students. Results of operations are accounted for during the summer months as the study programs are completed and students return to the United States. Consequently, all income and costs are deferred during the first nine months of the year. As a result, the unaudited nine month figures in the consolidated statement of earnings exclude any operations of New England Travel Corporation.

(C) Figures for 1968 have been restated in certain instances to make their presentation consistent with current accounting practices. There was no material effect as a result of such restatement.

(D) Net sales and earnings as originally reported to stockholders in the annual reports for the years 1967 and 1968 and original prospectus for the year 1966 and the amounts as shown in the statement of earnings in this proxy statement are reconciled as follows:

	1966	1967	1968
Net sales:			
Originally reported	$ 573,259	$2,386,500	$ 4,989,446
Pooled companies reflected retroactively	2,084,915	3,266,360	6,552,449
Per statement of earnings	$2,658,174	$5,652,860	$11,541,895
Net earnings (loss):			
Originally reported	(4,510)	168,616	388,031
Pooled companies reflected retroactively	80,059	217,019	385,121
Per statement of earnings	$ 75,549	$ 385,635	$ 773,152

(E) National Student Marketing Corporation has not paid any dividends except for $20,000 paid to the sole stockholder in connection with a reorganization prior to the shares of common stock of the company becoming publicly held.

Comments on Consolidated Statement of Earnings of National Student Marketing Corporation and Subsidiaries

The Company's subsidiary, Impressions by M Inc. did not begin to sell products until 1967. Therefore, since 1968 was the first full year of operations, there was a substantial increase in sales for the year ended August 31, 1968. As a result, because of the relatively low gross profit margin on these sales, which is characteristic of the industry, the cost of product sales increased from 39% to 60% as compared to an increase in product sales to 50% of total Company sales.

As explained in note B-3 of notes to consolidated statement of earnings, all revenues and expenses of the Company's subsidiary, New England Travel Corporation, are deferred during the first nine months of the year and accounted for during the last quarter. As a result, gross revenues increased substantially during the last quarter of 1968 as compared to the first nine months of that year. However, because the profit margin of these sales is lower than the average of the other companies included in the consolidated statement of earnings, net earnings do not reflect a proportionate increase.

During the second and third quarters of 1969, twenty-three middle management personnel were hired both to stabilize present operations and in expectation of future growth. The cost of expanding management personnel, along with interest cost of $200,000 incurred by borrowing $5,000,000, of which $3,000,000 was used for the acquisition of Guest Pac and $2,000,000 to finance internal growth, had an adverse effects on net earnings for the nine months ended May 31, 1969.

Form 280 A. -Affidavit of Service by Mail

AFFIDAVIT OF MAILING

State of New York)
County of New York)

Patricia D. Burks being duly sworn deposes and says that he is employed in the office of the United States Attorney for the Southern District of New York.

Stating also that on the 7th day of April, 1975 he served a copy of the within Memorandum by placing the same in aproperly postpaid franked envelope addressed: Morrison, Paul, Stillman & Beilley- 110 East 59th St NYC
Martin, Obermaier & Morvillo-1290 Ave of Amer. NYC
Cahill, Gordon & Reindel-80 Pine St. NYC
Cravath, Swaine & Moore-1 Chase Manhattan Plaza-NYC
2 copies each

And deponent further says that he sealed the said envelope and placed the same in the mailbox for mailing at the United States Courthouse, Foley Square, Borough of Manhattan, City of New York

Patricia D. Burks

Sworn to me before this

7th day of April, 1975

Jeanette Ann Grayeb

JEANETTE ANN GRAYEB
Notary Public, State of New York
No. 24-1541575
Qualified in Kings County
Commission Expires March 30, 1977